

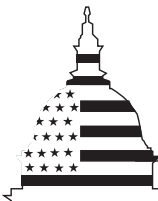
GAO

Report to the Chairman, Subcommittee  
on Oversight, Committee on Ways and  
Means, House of Representatives

March 2001

# WORK OPPORTUNITY TAX CREDIT

## Employers Do Not Appear to Dismiss Employees to Increase Tax Credits



G A O

Accountability \* Integrity \* Reliability

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Abbreviations

AFDC	Aid to Families With Dependent Children
CPS	Current Population Survey
EIN	Employer identification number
IRS	Internal Revenue Service
TANF	Temporary Assistance for Needy Families
WOTC	Work Opportunity Tax Credit



United States General Accounting Office  
Washington, DC 20548

March 13, 2001

The Honorable Amo Houghton  
Chairman, Subcommittee on Oversight  
Committee on Ways and Means  
House of Representatives

Dear Mr. Chairman:

The Work Opportunity Tax Credit (WOTC) is intended to increase the employment and earnings of workers belonging to certain disadvantaged groups by providing employers with an incentive to hire and retain these workers. However, as government and academic analysts have pointed out, the credit may also create incentives for employers to dismiss workers who do not make the employer eligible for the credit. Specifically, employers can increase their tax credit by dismissing workers for whom the employer has never received a tax credit in order to hire other workers who make the employer eligible for a credit; this practice is called displacement. Employers can also increase their tax credit by dismissing workers whose eligibility for the credit has ended and hiring other workers who make the employer again eligible for a credit; this practice is called churning.

Little is known about the employers who participate in the WOTC program or about participating employers' motivations for hiring and retaining workers for whom the employers can receive a tax credit. As agreed with your office, our objectives in this study were to determine (1) the characteristics, including motivations, of the employers who have participated in the credit program and (2) the extent, if any, to which employers have practiced displacement or churning.

To determine the characteristics of employers, we analyzed nationwide data from IRS on the use of the WOTC and data from agencies in California and Texas on the number of WOTC-certified employees hired by each employer.<sup>1</sup> To obtain information relating to the extent of churning and displacement, we (1) surveyed a probability sample of employers who

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<sup>1</sup>State agencies are responsible for determining the eligibility of individuals as members of targeted groups and issuing certifications of eligibility to the employers of those individuals.

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participated in the credit program in California and Texas and (2) analyzed data from agencies in these two states on the actual earnings and employment histories of certified employees. We chose California and Texas primarily because they are among the states that certified the largest number of employees to participate in the WOTC program in fiscal year 1999 and have electronic databases of their WOTC program data. We did not evaluate the effectiveness or efficiency of the WOTC in promoting the hiring of disadvantaged individuals. For example, we did not determine the extent to which employers may have received “windfall” credits for employees whom they would have hired anyway. Our methodology is described further in the scope and methodology section of this letter and in appendix I. Our survey instruments are reproduced in appendix II.

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## Results in Brief

Large employers earned most of the credit and hired most of the employees under the Work Opportunity Tax Credit program. In 1997, 4,465 corporations earned a total of \$135 million in tax credits. The employers who earned most of the credit were large companies, with gross receipts of \$1 billion or more, and engaged in nonfinancial services and retail trade. Our analysis of state agency data for California and Texas from 1997 through 1999 showed that 3 percent of participating employers accounted for about 83 percent of all hires of WOTC-certified employees. According to our survey, many employers who participated in the credit program in those two states in 1999 said that, besides the opportunity to obtain the credit, their participation in the program was also greatly influenced by such factors as the need to address a labor shortage (an estimated 36 percent) and the opportunity to be a good corporate citizen (an estimated 41 percent).

Although we were unable to definitively determine the extent to which displacement and churning occur, our review suggests that churning is likely to be very limited, if it occurs at all. Our survey of employers in two states indicates that 93 percent of participating employers said that displacement and churning have little or no cost-effectiveness. According to our survey, those employers estimated that the WOTC offset, on average, 47 percent of employers’ costs of recruiting, hiring, and training certified workers. If employers were practicing churning, it would make the most sense for them to dismiss their WOTC-certified employees near the earnings level (\$6,000) that would yield the maximum credit. Data from agencies in California and Texas on the employment of WOTC-certified employees showed that their employment rarely ends near that earnings level. These data also showed that certified workers with

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earnings within plus or minus \$1,000 of the \$6,000 credit-maximizing level were no more likely to separate from their employers than other certified workers, whose earnings fell short of or exceeded this range. The agency data did not allow us to perform similar tests for the occurrence of displacement, but we would not expect employers to undertake a practice that they said was not cost-effective. Because the results of both our survey and our analyses of employment data were similar for California and Texas, and because many of the firms employing the bulk of WOTC employees in these two states operate in multiple states, we believe the results of our two-state analysis indicate a low probability of displacement and churning in other states as well.

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## Background

The WOTC is intended to encourage employers to hire individuals from eight targeted groups that have consistently high unemployment rates. The targeted groups are

- individuals in families currently or previously receiving welfare benefits under the Temporary Assistance for Needy Families (TANF) program or its precursor, the Aid to Families With Dependent Children (AFDC) program;
- veterans in families currently or previously receiving assistance under a food stamp program;
- food stamp recipients—aged 18 through 24 years—in families currently or previously receiving assistance under a food stamp program;
- youth—aged 18 through 24 years—who live within an empowerment zone or enterprise community;<sup>2</sup>
- youth—aged 16 and 17 years—who live within an empowerment zone or enterprise community and are hired for summer employment only;
- ex-felons in low-income families;
- individuals currently or previously receiving Supplemental Security Income; and
- individuals currently or previously receiving vocational rehabilitation services.

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<sup>2</sup>Empowerment zone and enterprise community refer to an area or combination of areas designated by the U.S. Department of Housing and Urban Development or the U.S. Department of Agriculture that meet certain population, size, and poverty criteria. Effective for the period beginning January 1, 2002, the Community Renewal Tax Relief Act of 2000 (P.L. 106-554) expands this target group and the target group of youth employed during the summer to include qualified individuals who live in a renewal community that is designated by the Secretary of Housing and Urban Development.

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Additional eligibility criteria apply to these groups. For example, welfare recipients must have received AFDC or TANF benefits for any 9 months during the 18-month period ending on the hiring date in order to be eligible for the program.

The amount of tax credit that employers can claim under this program depends upon how long they retain credit-eligible employees and the amount of wages they pay to WOTC-certified employees. Employers who retain certified employees for at least 120 but less than 400 hours qualify for a credit of 25 percent of up to \$6,000 in wages, for a maximum credit of \$1,500. Employers who retain certified employees for 400 hours or more qualify for a credit equal to 40 percent of up to \$6,000 in wages, for a maximum credit of \$2,400.<sup>3</sup> The credit is calculated using the actual first year wages paid or incurred. Employers must reduce their tax deductions for wages and salaries by the amount of the credit. In addition, as part of the general business credit, the WOTC is subject to a yearly cap.<sup>4</sup> However, excess WOTC can be used to offset tax liabilities in the preceding year or in any of 20 succeeding years.

The WOTC was first authorized in the Small Business Job Protection Act of 1996 to improve upon and replace a similar, expired program—the Targeted Jobs Tax Credit program.<sup>5</sup> The WOTC was designed to mitigate some shortcomings that had been identified in the previous credit program—specifically, that it gave employers windfalls for hiring employees that they would have hired anyway and that too many credit-eligible employees left their jobs before they received much work experience. Some target groups were reformulated with the intention of focusing narrowly on those who truly need a credit for firms to risk hiring them. In addition, the minimum employment period for receiving the higher rate of credit was lengthened. The WOTC became effective

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<sup>3</sup>The tax credit for youths in summer jobs has a lower wage limit than that for the other target groups. See appendix III for a detailed description of the limit on credit-eligible wages for youths in summer jobs.

<sup>4</sup>The general business credit combines several tax credits, including the WOTC, for the purpose of computing an overall dollar limitation on the reduction of tax liability. The general business credit may not exceed net income tax minus the greater of (1) the tentative minimum tax or (2) 25 percent of the net regular tax liability above \$25,000.

<sup>5</sup>Small Business Job Protection Act (P.L. No. 104-188).

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beginning in October 1996 and has since been reauthorized. It is due to expire in December 2001.

In fiscal year 1999, 335,707 individuals were certified as members of the targeted groups, making their employers eligible for the credit if the workers remained on the job for at least 120 hours. Individuals in the welfare target group made up 54 percent of the individuals certified. Youth in the food stamp target group made up another 20 percent of the individuals certified. The other six target groups each accounted for 1 to 8 percent of the remaining certifications.

Federal and state agencies share responsibility for administering the WOTC program. The Department of the Treasury, through the Internal Revenue Service (IRS), is responsible for the tax provisions of the credit. The Department of Labor, through the Employment and Training Administration, is responsible for developing policy and program guidance and providing oversight of the WOTC program. In addition, the Department of Labor awards grants to states for administering the eligibility determination and certification provisions of the program. State agencies verify and report to the Department of Labor on state certification activities. All 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands participate in the program. Neither the Department of the Treasury nor the Department of Labor regulations require these agencies to take any actions regarding displacement or churning.

The State of New York and the Department of Labor have undertaken studies that may have findings relevant to whether employers engage in displacement or churning practices. The New York study, which was issued in 1998, concluded, among other things, that employer windfalls from churning employees are minimal. This conclusion was based on analysis of state WOTC and Wage Reporting databases with records on 12,609 individuals in New York covering the fourth quarter of 1996 through the first quarter of 1998. The study did not address displacement. The Department of Labor study is ongoing, so its results are not yet available. The study is using in-depth interviews with 16 employers who hire a large number of employees under the WOTC program to examine the hiring, retention, and career advancement experiences of WOTC employers and employees.



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## Scope and Methodology

To obtain information on the characteristics of employers, we analyzed national tax data from the IRS' Statistics of Income Division for 1997, the most recent year that data were available, and state WOTC data from agencies in California and Texas for 1997 through 1999. To obtain information relating to the extent of displacement and churning, we surveyed a stratified probability sample of employers who have participated in the WOTC program in California and Texas. The participating employers that we surveyed are those with repeated and recent experience in the program in that they hired at least one WOTC employee in 1999 and hired at least one WOTC employee in another year. Our sample is projectible to the entire population of 1,838 employers in California and Texas who met these hiring criteria.

For information relating to churning, we also analyzed WOTC and unemployment insurance data for these states. With these data, we determined the total earnings and length of employment of WOTC-certified employees and examined this information for evidence concerning the extent and likelihood of churning.

For additional information relating to displacement, we analyzed national employment data in the Commerce Department's Current Population Survey (CPS) for 1995 through 1999. We used the CPS data to estimate employment rates for members of groups targeted by the credit and members of groups not targeted by the credit but who may substitute in employment for target group members. The absence of a centralized database containing the necessary detailed information precluded a nationwide survey of employers and analysis of employment practices.

We chose California and Texas because they are among the states that

- certified the largest number of employees to participate in the WOTC program in fiscal year 1999,
- have electronic databases of their WOTC program data, and
- provided a somewhat geographically diverse population.

Together, California and Texas certified about 12 percent of WOTC-eligible individuals in fiscal year 1999, ranking them second and fifth, respectively, in WOTC certifications for that fiscal year. When reporting our estimates derived from the sample and our analysis of program and unemployment insurance data, we combined data from both states because the results in the two states were similar. Furthermore, the confidence intervals for all point estimates in the letter of this report are no more than 10 percentage points on either side of the estimate.

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Our survey and state agency data pertain only to participating employers in California and Texas. However, to assure ourselves that our findings are likely to apply to WOTC employers in the rest of the nation, we examined the federal laws and regulations related to the credit, surveyed state administrators responsible for the credit, and analyzed the data on participating employers. The federal tax benefits offered by the WOTC are the same across all states. Therefore, we have no reason to believe that employers in California and Texas respond differently to these incentives than employers in other states. We spoke to the officials who were responsible for administering the WOTC program in all 50 states, and they all confirmed that their states made no effort to either encourage or discourage displacement or churning. From the participating employer data, we determined that employers who operate in multiple states account for most of the WOTC hires in California and Texas. Moreover, we found no differences relevant to churning and displacement between employers in California and Texas in the results of our survey and agency data analyses, suggesting that our conclusions would be generalizable to employers in other states as well.

We did not evaluate how effective or efficient the WOTC has been in increasing the employment and earnings of target group members. To do this, we would have had to determine the extent to which

- the credit caused employers to hire workers that they would not otherwise have hired,
- employees' experience with WOTC employers increases their current and future earnings, and
- employers received "windfall" credits for employees whom they would have hired anyway.

We did not address any of those issues in this report.

We did not verify the state and federal databases we used. However, agreements between the Department of Labor and state WOTC offices require the states to conduct audits of the accuracy of their WOTC records. A review of studies of the accuracy of unemployment insurance data, which was conducted for the National Research Council, concluded that the data appear to be accurate. The study notes that employers are required by law to report the data and that intentional inaccuracies are subject to penalties. This same review of studies found that the CPS data are a valuable source of information on the national low-income population, with broad and fairly accurate measures of income. However, the study noted that sample sizes may be small for some subpopulations

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(e.g., welfare recipients in particular states), and the percentage of some subpopulations covered by the survey appears to have declined modestly in recent years. The tax data from IRS' Statistics of Income Division undergo numerous quality checks but do not include information from amended tax returns.

We conducted our review from January 2000 through December 2000 in accordance with generally accepted government auditing standards. Our scope, methodology, and the sources of the data we used are discussed further in appendix I. We requested comments on a draft of this report from the Department of Labor and asked cognizant agencies in California and Texas to review the draft's discussion of their WOTC efforts. The comments are discussed near the end of this letter.

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## Large Employers Made the Most Use of the Credit

Employers who were large in terms of gross receipts earned most of the credit reported in 1997, the latest year for which data were available. Data from the agencies that certify WOTC employees in California and Texas showed that a relatively small number of employers did most of the hiring in the WOTC program from 1997 through 1999. Employers' participation in the program was greatly influenced by such factors as the opportunity to obtain the credit, address a labor shortage, and be a good corporate citizen.

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## Large Employers in a Few Industries Earned Most of the Credit

In 1997, nationwide, an estimated 4,465 corporations earned an estimated total of \$134.6 million in tax credits.<sup>6</sup> Approximately 66 percent of the credit was earned by corporations with gross receipts of \$1 billion or more. Table 1 shows the amount of credit that businesses earned by amount of gross receipts.

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<sup>6</sup>The credit data we present include the amount earned by subchapter S corporations. A subchapter S corporation is treated similarly to partnerships for federal income tax purposes. Shareholders claim the credit on their individual tax returns. Aside from these shareholders, a negligible amount of credit was earned by individual taxpayers.

**Table 1: Distribution of Businesses Earning WOTC and the Amount of Credit Earned by Size of Gross Receipts, Nationwide in 1997**

Dollars in millions

Gross receipts	Businesses		Credit earned	
	Number	Percent	Amount	Percent
\$0 – less than \$1	1,577	35.9	\$6.5	4.8
\$1 – less than \$10	1,494	33.5	7.0	5.2
\$10 – less than \$50	643	14.4	7.0	5.2
\$50 – less than \$100	133	3.0	2.3	1.7
\$100 – less than \$250	160	3.6	5.5	4.1
\$259 – less than \$500	118	2.7	8.4	6.2
\$500 – less than \$1,000	106	2.4	9.4	7.0
\$1,000 and greater	232	5.2	88.5	66.3
<b>Total</b>	<b>4,465</b>	<b>100.0</b>	<b>\$134.6</b>	<b>100.0</b>

Note: Columns may not sum to totals because of rounding.

Source: GAO analysis of IRS data.

Most of the credit was reported by businesses engaged in nonfinancial services, such as hotel, motel, and other personal services, and retail trade. These industries accounted for 81 percent of the credit reported. Table 2 shows the credit amounts earned by businesses in each industry in 1997. The aggregate amount of WOTC earned by taxpayers is likely to have grown significantly between 1997 and 1999 because the number of WOTC certifications grew significantly nationwide over that period—from 126,113 to 335,707. However, based on the certification data we have from California and Texas, we believe that the percentage distribution of the credit by size of employer and by industry has not changed dramatically. The size distribution of employers measured by number of WOTC hires did not change significantly in either California or Texas during that period. The distribution of certifications by industry also changed little in Texas; we do not have industry information for California.

**Table 2: Distribution of Businesses Earning WOTC and the Amount of Credit Earned, by Industry, Nationwide in 1997**

Dollars in millions

Industry	Businesses		Credit earned	
	Number	Percent	Amount	Percent
Construction	760	17.0	\$2.7	2.1
Manufacturing	649	14.5	15.8	11.8
Transportation and public utilities	25	0.6	3.6	2.7
Wholesale trade	126	2.8	1.3	1.0
Retail trade	1,057	24.1	75.0	55.8
Finance, Insurance and Real Estate	342	7.7	2.0	1.5
Nonfinancial Services	1,480	33.2	33.7	25.0
Other	9	0.2	0.3	0.2
<b>Total</b>	<b>4,465</b>	<b>100.0</b>	<b>\$134.6</b>	<b>100.0</b>

Note: Columns may not sum to totals because of rounding.

Source: GAO analysis of IRS data.

### A Relatively Small Number of Employers Accounted for Most WOTC Hires in California and Texas

Our analysis of WOTC certification data in California and Texas for 1997 through 1999 showed that a few employers did most of the hiring in the WOTC program. Employers who hired more than 100 WOTC-certified employees represented about 3 percent of all employers in the program but accounted for about 83 percent of all hires. About 65 percent of employers in the program made only one WOTC hire.

The larger WOTC employers spent more time in the program. Employers who hired more than 100 WOTC-certified employees were in the program for an average of 10 or more quarters, while those hiring 5 or fewer employees were in the program for an average of less than 3 quarters. The larger WOTC employers also hired more frequently. Employers who hired in every year accounted for about 83 percent of total hires while representing about 8 percent of all employers. Table 3 shows the distribution of the number of employers, the number of WOTC-certified employees, and time in the program, by size of employers (in terms of WOTC-certified hires) for 1997 through 1999.

**Table 3: Distribution in Texas and California of Number of Employers, Number of WOTC Hires, and Average Time in the Program, by Size of Employer, 1997-99**

Size in terms of WOTC hires	Employers		WOTC hires		Average time <sup>a</sup>
	Number	Percent	Number	Percent	
1	4,220	64.5	4,220	2.6	0.2
2 – 5	1,265	19.3	3,573	2.2	2.8
6 – 10	279	4.3	2,210	1.4	5.8
11 – 15	133	2.0	1,708	1.1	6.7
16 – 20	97	1.5	1,734	1.1	7.4
21 – 25	53	0.8	1,207	0.7	7.0
26 – 50	159	2.4	5,661	3.5	8.6
51 – 100	116	1.8	8,113	5.0	9.3
101 – 200	101	1.5	14,150	8.7	10.4
201 – 500	63	1.0	20,189	12.4	10.8
Greater than 500	59	0.9	99,823	61.4	12.1
<b>Total</b>	<b>6,545</b>	<b>100.0</b>	<b>162,588</b>	<b>100.0</b>	<b>1.7</b>

Note: Totals may not sum because of rounding.

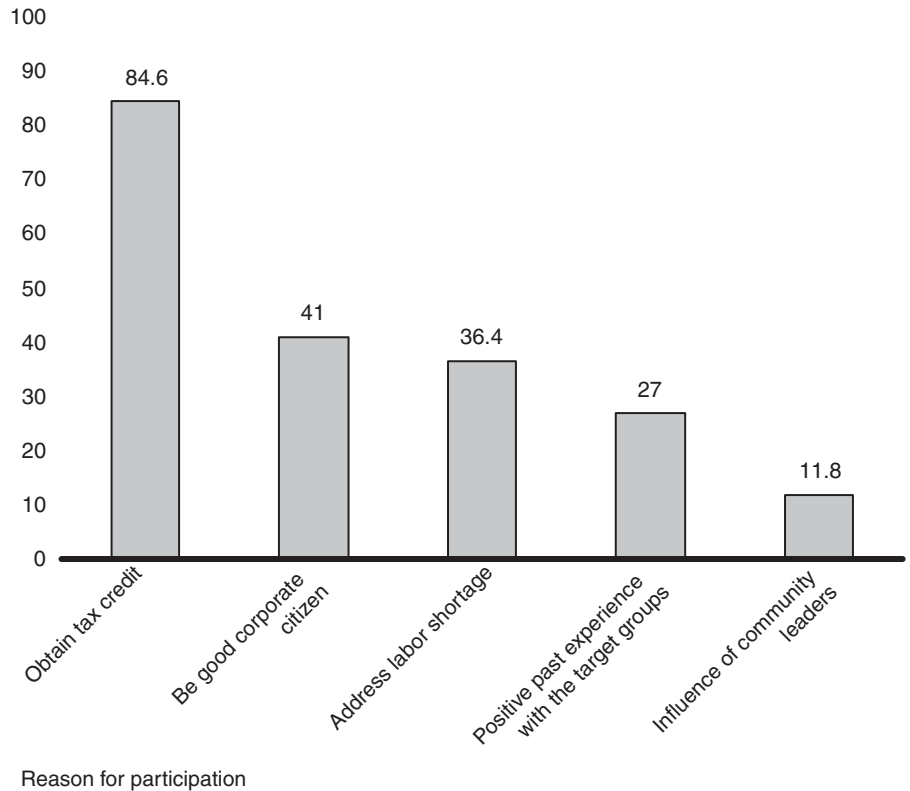
<sup>a</sup>Time in quarters.

Source: GAO analysis of California and Texas WOTC databases.

## Several Factors Influenced Participation in the WOTC Program

The employers that we surveyed in two states reported that the opportunity to obtain a tax credit was by far the factor that most influenced their decisions to participate in the WOTC program, followed by the opportunity to address labor shortages and be a good corporate citizen. According to our survey, the opportunity to obtain the credit was the largest influence, with an estimated 85 percent of participating employers in California and Texas saying they were greatly influenced by this opportunity. Figure 1 shows the extent to which employers in the states we reviewed said that specific factors greatly influenced their participation in the program.

**Figure 1: Factors Greatly Influencing Employer Participation in California and Texas**  
Estimated percentage



Source: GAO analysis of survey data.

Participation in the program appears often to have had support from high levels within the companies. For example, for an estimated 57 percent of California and Texas employers, the possibility of participating in the program was raised by someone inside the company rather than by an outside organization. In those situations, high-level management was responsible for raising the idea of participating in the WOTC program about three-quarters of the time, according to our survey-based projections.

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## If Displacement and Churning Occur, They Are Likely to Be Very Limited

Displacement and churning are likely to be limited, if they occur at all, because, as our survey of employers in California and Texas indicates, most employers view these practices as having little or no cost-effectiveness. This view is consistent with the employers' estimate that the credit offsets less than half the costs of recruiting, hiring, and training credit-eligible employees. Our employer survey also indicates that most vacancies filled by credit-eligible employees occur for reasons unrelated to displacement and churning, such as voluntary separations. Furthermore, our survey indicates that most employers change at least one recruitment, hiring, or training practice, which, studies suggest, may make these employers more likely to retain new hires. Our analysis of program and employment data from state agencies supports what we learned from the survey regarding the low probability of churning. These data show that employment rarely ends near the earnings level that yields the maximum credit, and employees earning the maximum are no more likely to separate than are other WOTC-certified employees. The agency data do not allow us to perform similar tests for the occurrence of displacement. However, displacement is less likely to occur when employers are increasing their workforce—as has been the case since the introduction of the credit—because they have less need to dismiss non-WOTC workers in order to hire WOTC workers.

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## California and Texas Employers View Displacement and Churning as Not Cost-Effective

Most employers do not consider displacement and churning to be cost-effective employment practices. Based on our survey, we estimate that 93 percent of participating employers in California and Texas would agree that displacement is cost-effective to little or no extent. An estimated 93 percent of employers also hold that view regarding churning. Displacement and churning are not cost-effective if the cost of recruiting, hiring, and training a new employee exceeds the amount of WOTC that an employer expects to earn from that employee. Under those circumstances, the WOTC provides no incentive for that employer to dismiss an existing employee to hire a WOTC-certified one. According to our employer survey, on average, the tax credit offsets less than one-half (47 percent) of this



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cost.<sup>7</sup> Furthermore, employers told us that it is important to reduce the turnover of WOTC-certified employees. Based on our survey, we estimate that for 71 percent of participating employers in those two states, retaining employees after the maximum tax credit has been secured is very important. An additional 20 percent would view retention of employees after the maximum tax credit is secured as somewhat important.

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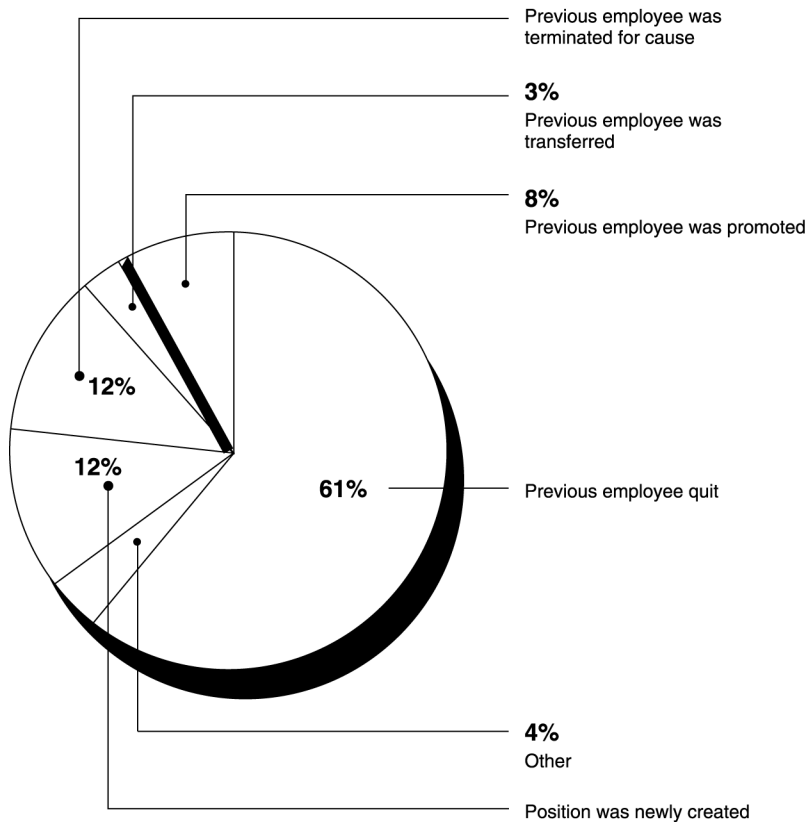
### Participating Employers Reported, on Average, That Most Vacancies Result From Voluntary Separations

For those employers who could tell us the reasons for the vacancies that were filled by WOTC-certified employees, an estimated average of 61 percent of such vacancies arose because the previous employees quit. On average, the next most frequent reasons for the vacancies were that the previous employees were terminated for cause and that the positions were newly created. Figure 2 shows the distribution by California and Texas employers' responses regarding the reasons for vacancies. None of the reasons given were related to displacement or churning.

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<sup>7</sup>Although the WOTC does not appear to provide an incentive for employers to purposely create vacancies for credit-eligible employees by dismissing existing employees, the credit may, nevertheless, provide an incentive for employers who already have vacancies to fill them with credit-eligible employees. According to our survey, the difference between the average cost of recruiting, hiring, and training a credit-eligible employee (\$3,799) and the average cost of the same activities for a noneligible employee (\$3,265) is not statistically significant. Therefore the credit may more than offset any additional cost associated with choosing a credit-eligible individual over a noneligible individual to fill an existing vacancy. (The maximum credit is \$2,400, but most WOTC-certified employees leave their jobs well before the maximum credit is reached. See the data presented later in this report). We did not attempt to determine whether the WOTC is effective in encouraging employers to hire individuals from the target populations (see the scope and methodology section of this report). However, we did determine that, for an estimated 70 percent of participating employers in the two states, the tax credit's insufficiency to offset recruitment, hiring, and training costs has little or no deterrent effect on employer willingness to fill vacancies with credit-eligible individuals.

**Figure 2: Reported Reasons for Vacancies Filled by WOTC-Eligible Hires in California and Texas**



Note 1: We asked each employer what percentage of these vacancies was due to each of the reasons listed in the figure. We then averaged those percentages across responding employers.

Note 2: The “other” category included responses such as “seasonal hiring buildup” and “additional workforce needed.”

Source: GAO analysis of survey data.

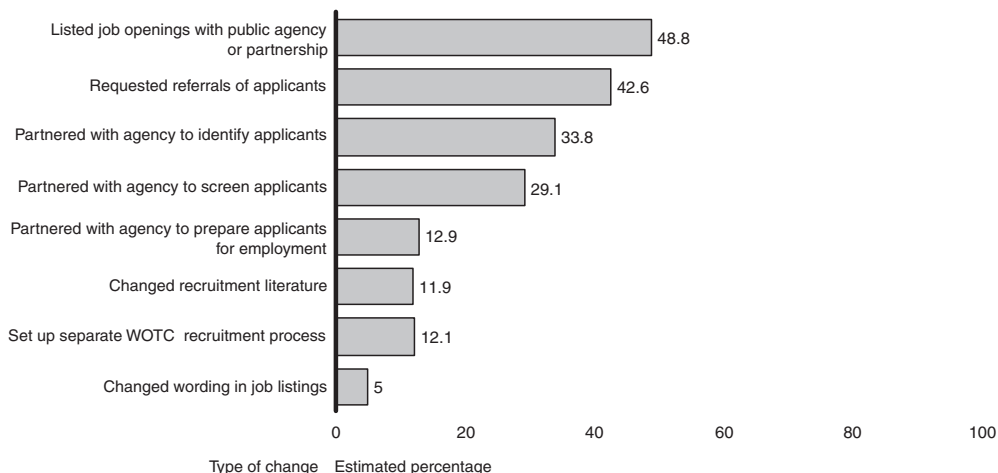
### Most Participating California and Texas Employers Changed Recruiting, Hiring, or Training Practices

About 85 percent of employers in California and Texas have changed a recruiting, hiring, or training practice to secure the WOTC and better prepare credit-eligible new hires, according to estimates that are based on employer-reported information from our survey. Furthermore, an estimated 43 percent of employers in these two states have changed their practices in all three of these areas. A 1999 study conducted by Jobs for the Future found that employers who successfully employed welfare recipients—which is the largest targeted group in the WOTC program—developed strategies to improve access, retention, and advancement of

those individuals.<sup>8</sup> The strategies used by employers in our survey included targeted recruitment; outreach and screening assistance from organizations that know and understand the targeted group; pre-employment training, such as training in communication skills; and mentors, among other strategies. These strategies are consistent with ones these researchers identified in other studies.

Based on the results of our survey, we estimate that about two-thirds of participating employers in the two states changed at least one recruitment practice to secure the tax credit. The most frequent change in recruitment practice was that employers listed job openings with a public agency or partnership. An estimated 49 percent of participating employers in the two states took such an action. Figure 3 shows the extent to which participating employers changed recruitment practices to secure the credit.

**Figure 3: Percentages of Participating Employers in California and Texas Who Changed Recruitment Practices to Secure the Credit**

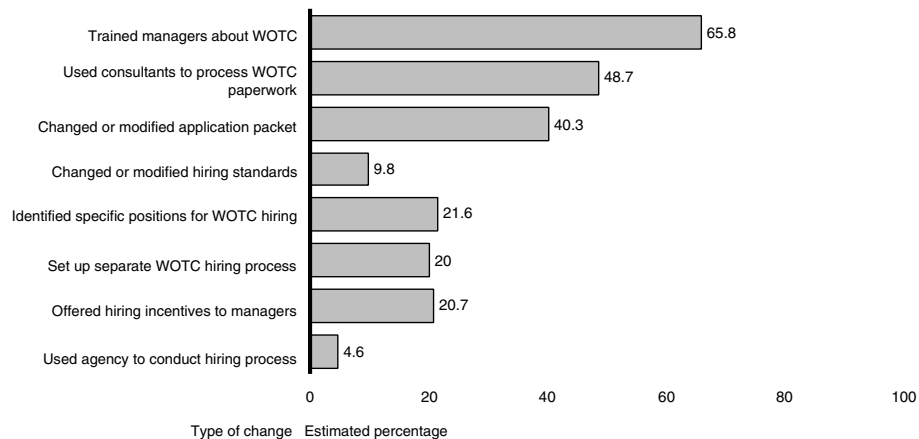


Source: GAO analysis of survey data.

<sup>8</sup>*Business Participation in Welfare-to-Work: Lessons from the United States*, (Boston: Jobs for the Future, 1999). Jobs for the Future is a national nonprofit organization that focuses on workforce development issues.

An estimated three-quarters of participating employers in the two states changed at least one hiring practice to secure the tax credit. Our survey indicated that the most frequent change in hiring practices was that employers began training their managers about the tax credit, with an estimated 66 percent of employers making that change. Figure 4 shows the extent to which participating employers changed hiring practices to secure the credit.

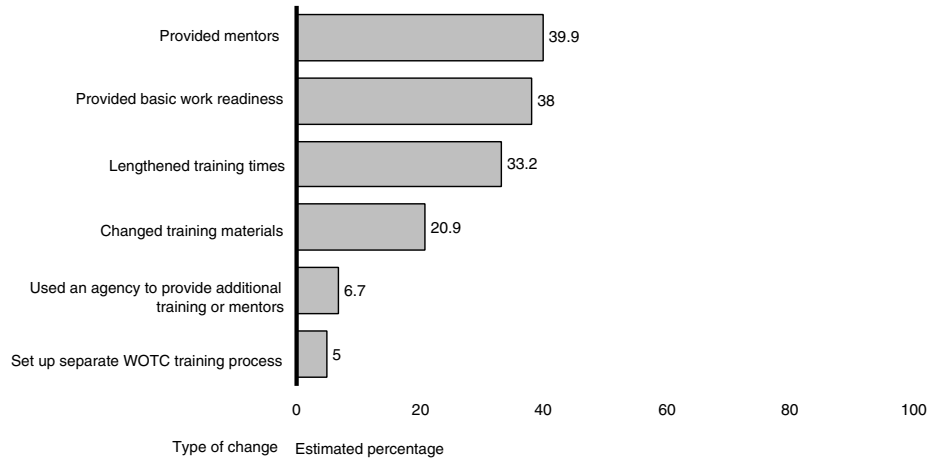
**Figure 4: Percentages of Participating Employers in California and Texas Who Changed Hiring Practices to Secure the Credit**



Source: GAO analysis of survey data.

Based on our survey, we estimate that about one-half of participating California and Texas employers changed at least one training practice to better prepare WOTC new hires. For example, an estimated 40 percent began providing mentors to their new hires. Figure 5 shows the extent to which participating employers changed training practices to secure the credit.

**Figure 5: Percentages of Participating Employers in California and Texas Who Changed Training Practices to Secure the Credit**



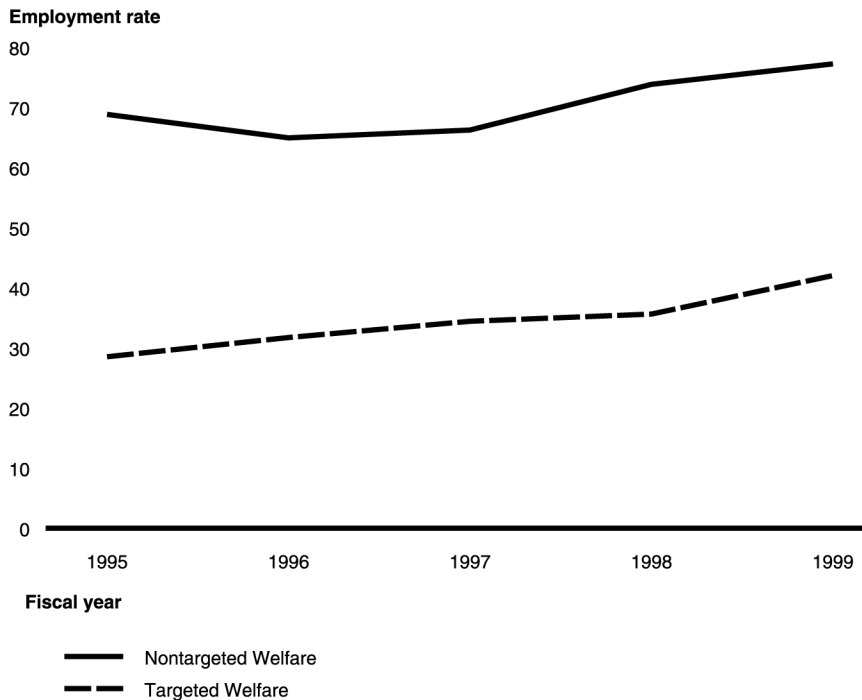
Source: GAO analysis of survey data.

## Robust Employment Growth Makes Displacement Less Likely

Displacement is less likely to occur when employers are increasing their workforce because they have less need to dismiss non-WOTC workers in order to hire WOTC workers. Since the introduction of the credit in the last quarter of 1996, employment in the U. S. economy has grown robustly, even for low-skilled workers. Using the CPS data, we found that employment rates grew over the period for certain target group members and closely related nontarget group members that may substitute in employment for the target groups. For example, we estimated employment rates for welfare recipients in the CPS (those on welfare for 9 or more months in the previous year) who would be members of the group targeted by the credit.<sup>9</sup> We also estimated employment rates for welfare recipients who would not be target group members (those on welfare less than 9 months of the previous year). The employment rate of the target group welfare recipients grew by 47 percent and nontarget welfare recipients by 12 percent from 1995 through 1999. Figure 6 shows employment rates over the period for members of the targeted and nontargeted welfare groups.

<sup>9</sup>The welfare target group is members of families receiving benefits under TANF or AFDC for any 9 of the last 18 months, ending on the hiring date. The data elements in the CPS permit us to identify most, but not all, of the welfare target group members in the CPS database.

**Figure 6: Employment Rates of Targeted and Nontargeted Welfare Recipients, 1995-99**

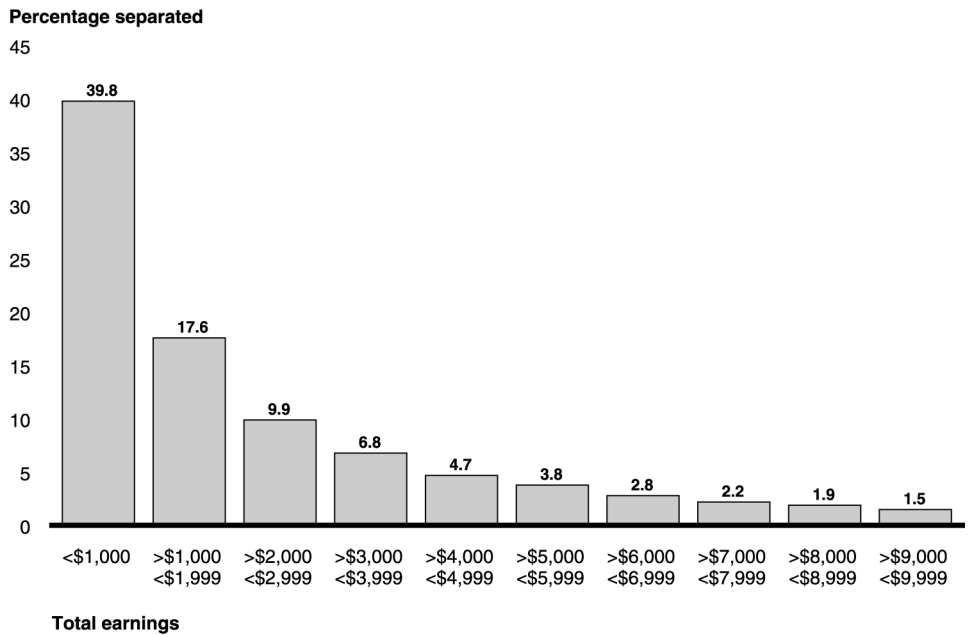


Source: GAO analysis of CPS data.

### Relatively Few WOTC Hires Are Still Employed When Churning Is Most Likely

Our analysis of the WOTC and unemployment insurance data in California and Texas showed that most certified employees do not earn enough income while working for WOTC employers for churning to make sense for those employers. Sixty-seven percent of certified employees separated from their employers after earning less than \$3,000. Furthermore, only a relatively small number of certified employees earned incomes in the range where churning may be most likely to occur. Employers wishing to maximize their credit would retain WOTC employees until they had earned a total of \$6,000, the maximum earnings eligible for the credit. Only about 7 percent of certified employees separated after earning incomes between \$5,000 and \$7,000 (a range of earnings within \$1,000 of the credit maximizing level). If employers did not churn when employees reached this level of earnings, it seems less likely that they would churn at other levels of earnings. Figure 7 shows the percentage of employees separating after earning a given amount of income.

**Figure 7: Separation Rates for Certified WOTC Employees in California and Texas, by Earnings, 1997-99**



Note: The figure does not include the 9 percent of employees who earned \$10,000 or more while working for the WOTC employer. Including these employees would require extending the figure with numerous additional \$1,000 total earnings categories. However, the shape of the figure would be unchanged because the certified employees in each of these additional categories would represent less than 2 percent of total certified employees.

Source: GAO analysis of Texas and California WOTC and Unemployment Insurance databases.

**Employees Who Reached the Maximum Earnings in California and Texas Were No More Likely to Separate From WOTC Employers Than Those Who Do Not**

In addition to determining the percentage of WOTC-certified employees who separated near the maximum earnings level, we also analyzed the effect of reaching the maximum earnings level on the likelihood of separation. We used a statistical technique to measure the likelihood of separation of WOTC-certified employees who reach the maximum earnings level in a given quarter relative to the likelihood of separation of WOTC-certified employees who do not reach the maximum. The technique that we used allows us to measure the effect on the likelihood of separation, while controlling for the effects of other employee characteristics, such as membership in a particular target group. The measured effect is, therefore, the net effect on the likelihood of separation (i.e., net of the effects of the other characteristics).

Using this technique, our analysis showed that WOTC-certified employees who reach the maximum earnings in a given quarter (i.e., those whose

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cumulative earnings are between \$5,000 and \$7,000) are no more likely to separate from their WOTC employers than those employees who do not reach the maximum. In addition, the analysis showed that reaching the maximum has no effect on the likelihood of separation across most target groups. For example, members of the welfare target group are no more likely to separate in the quarter in which they reach the maximum than are members of other target groups who reach the maximum. Besides differences in target group membership, this analysis also controlled for differences in the occupation of employees, size of employers in terms of total employment, and other factors. This analysis is described in more detail in appendix III.

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## Conclusions

The fact that an overwhelming majority of WOTC employers whom we surveyed in California and Texas considered displacement and churning to have little or no cost-effectiveness leads us to conclude that few of them would engage in these practices. Our analyses of WOTC employment data compiled by the two states provides further support for this conclusion with respect to churning. Further, although our survey and state agency data pertain only to participating employers in California and Texas, we believe that our conclusions regarding the occurrence of displacement and churning are likely to hold true in the remainder of the nation. The federal tax benefits offered by the WOTC are the same across all states. Therefore, we have no reason to believe that employers in California and Texas would be less responsive to those incentives than employers in other states. Moreover, employers that operate in multiple states account for most of the WOTC hires in California and Texas. We spoke to the officials who were responsible for administering the WOTC program in all 50 states and they all confirmed that their states made no efforts to either discourage or encourage displacement or churning. The fact that there were no differences relevant to displacement and churning between the results of our survey and agency data analyses for California and those for Texas also gives credence to the generalizability of our conclusions.

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## Agency Comments

The Department of Labor sent e-mail comments on a draft of this report to us on March 1, 2001. The Department of Labor made suggestions for clarifying information in the report. We modified the report where appropriate. The Department of Labor also stated that, given the wealth of evidence in our report indicating that displacement and churning are limited, our conclusions regarding the use of these practices could be stronger. We did not strengthen our characterization of the extent to which displacement and churning may be occurring because we believe



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that our conclusion appropriately reflects the strength of our methodology and resulting data.

Agencies in California and Texas responsible for the WOTC program also reviewed our draft report regarding our description of the credit program in their state and our analysis of state data. The agencies stated that they had no suggestions for changes in our report.

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As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we are sending copies of this report to Representative William J. Coyne, Ranking Minority Member, Subcommittee on Oversight, House Committee on Ways and Means; the Honorable Elaine L. Chao, Secretary of Labor; the Honorable Charles O. Rossotti, Commissioner of Internal Revenue; Mark Heilman, Chief, Job Services Division, California Employment Development Department; and John Carlson, WOTC Coordinator, Texas Workforce Commission. Copies of this report will be made available to others upon request.

If you have any questions regarding this report, please contact me or James Wozny at (202) 512-9110. Key contributors to this report are acknowledged in appendix IV.

Sincerely yours,



Michael Brostek  
Director, Tax Issues

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# Appendix I: Objectives, Scope, and Methodology

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The objectives of this report were to determine (1) the characteristics of employers who have participated in the WOTC program and (2) the extent, if any, to which employers have practiced displacement and churning. To obtain information on the characteristics of employers, we analyzed national tax data from the Statistics of Income Division of the Internal Revenue Service for 1997, the most recent year that data were available, and state WOTC data from agencies in California and Texas for 1997 through 1999. To obtain information relating to the extent of displacement and churning, we surveyed a stratified probability sample of employers who have participated in the WOTC program in California and Texas. Our survey of employers is discussed in more detail below.

For information relating to churning, we also analyzed WOTC and unemployment insurance data for California and Texas. With these data, we determined the total earnings and length of employment of WOTC-certified employees and analyzed this information for evidence concerning the extent and likelihood of churning. Our methodology for this analysis is discussed in detail in appendix III. For additional information relating to displacement, we analyzed national employment data in the Commerce Department's Current Population Survey (CPS) for 1995 through 1999. We used the CPS to estimate employment rates for members of groups targeted by the credit and members of groups not targeted by the credit but who may substitute in employment for target group members.

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## Survey of Employers

To obtain information relating to the extent of displacement and churning, we identified participating employers from databases of employees who had applied for certification under the WOTC program. These databases are maintained by the state agencies in California and Texas that are responsible for determining the eligibility of employees as members of targeted groups and issuing certifications of eligibility to employers.

Our desired survey population initially was managers who were hiring WOTC program employees nationwide. However, since this information is kept by each state office in various forms, it was not feasible to assemble a national sampling frame. Therefore, we used data from two of the five states with the largest numbers of WOTC employee participants in 1999. California and Texas were the two states of the five largest with manageable electronic databases of WOTC employees in 1999. We identified employers from these lists by their unique employer identification numbers (EIN), which are used by IRS. In order to have a population of employers with repeated and recent experience with the program, we included only those who had hired at least one certified

employee, hired at least once in 1999, and hired at least once in 1997 or 1998.

To identify employers from the databases of WOTC-eligible employees, we aggregated the employees according to their employer’s EIN. For the purposes of our sample, we defined “employer” as a unique EIN and selected a stratified random sample of 157 employers from the 975 total employers in California and 148 employers from the 863 total employers in Texas.<sup>1</sup> The strata were defined by how many WOTC employees the employer hired. Because employers who had more than 100 WOTC hires accounted for 80 percent of the total WOTC hires, those employers hiring more than 100 employees were a separate stratum from those hiring between 2 and 100 WOTC employees. In this way, we were able to sample more employers with larger numbers of WOTC hires. Table 4 shows the breakdown by state and stratum of the number of employers in the population, the number selected into the sample, and the number who responded to the survey. In total, we sampled 305 employers and received responses from 225, for an overall response rate of 74 percent.

**Table 4: Number of Population and Sample Cases in Strata for Employers Hiring WOTC Employees**

<b>Stratum</b>	<b>2 to 100 hires</b>	<b>Over 100 hires</b>	<b>Total</b>
<b>California</b>			
Population	775	200	975
Selected	92	65	157
Completed survey	66	50	116
Percent completed	72%	77%	74%
<b>Texas</b>			
Population	610	253	863
Selected	86	62	148
Completed survey	71	38	109
Percent completed	83%	61%	74%

Source: GAO analysis of WOTC and survey data in California and Texas

<sup>1</sup>In California, there were 6,658 employers who filed requesting eligibility for their employees under the WOTC program. Of these, 975 met the criteria for inclusion in the population of hiring at least one employee who was certified as eligible, hiring in 1999, and hiring in at least one other year. In Texas, there were 4,240 employers who hired under the program, and 863 of these who met the criteria for inclusion in the population.

In addition to the EINs for the employers associated with WOTC-eligible employees, the databases included limited information for a contact person. To try to ensure that our surveys reached the correct person at the employer site, we contacted every sampled employer by phone first. In this initial phone call, we explained the purpose of the survey, the kinds of questions we would be asking, and the location for which we were interested in obtaining information, and we asked for the name of the most appropriate respondent. Most initial contacts indicated that they were the most appropriate respondent or that they would receive the survey and forward it as necessary. Approximately 4 weeks after the initial mailout, we conducted a second mailout to those who had not yet responded. Approximately 4 weeks after that, we followed up with all remaining nonrespondents by telephone, reminding them that they had not responded and asking them to complete a shorter version of the questionnaire over the telephone.

Because the survey results come from a sample, all results are estimates that are subject to sampling errors. These sampling errors measure the extent to which samples of these sizes and structure are likely to differ from the populations they represent. Each of the sample estimates is surrounded by a 95-percent confidence interval, indicating that we can be 95-percent confident that the interval contains the actual population value. Unless otherwise noted, the 95-percent confidence intervals for all percent estimates in the letter of the report do not exceed plus or minus 10 percentage points around the estimate.

In addition to the reported sampling errors, the practical difficulties of conducting any survey may introduce other types of error, commonly referred to as nonsampling errors. For example, differences in how a particular question is interpreted may introduce variability into our survey results that is difficult to measure. We conducted pretests of the survey to evaluate the wording of the questions. One particular source of nonsampling error unique to this survey involves the location to which that respondent's answers refer. In some cases, the employer or EIN that we selected corresponded to a very large corporation, and our contact was in a hiring division located outside the state or local office of interest. In the initial phone calls, the location of interest was specified; however, the respondent may have responded with a different location in mind or may have been unable to take into account variation in hiring practices across several local offices. Careful pretesting of the survey did not uncover such issues, but this possibility may lead to additional variation in our survey results.

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## Limitations of Our Analysis

Our survey and state agency data pertain only to participating employers in California and Texas. However, to assure ourselves that our findings are likely to apply to WOTC employers in the rest of the nation, we examined federal laws and regulations related to the credit, surveyed state administrators responsible for the credit program, and analyzed data on the participating employers. The federal tax benefits offered by the WOTC are the same across all states. Therefore, we have no reason to believe that employers in California and Texas respond differently to these incentives than employers in other states. We spoke to the officials who were responsible for administering the WOTC program in all 50 states, and they all confirmed that their states made no effort to either encourage or discourage displacement or churning. Moreover, employers that operate in multiple states account for most of the WOTC hires in California and Texas. We found no significant differences between employers in California and Texas in the results of our survey and agency data analyses, suggesting that our conclusions will be generalizable to employers in other states as well.

We did not verify the state and federal databases we used. However, agreements between the Department of Labor and state WOTC offices require the states to conduct audits of the accuracy of state WOTC records. A review of studies of the accuracy of unemployment insurance data conducted for the National Research Council concluded that the data appear to be accurate. The review noted that employers are required by law to report the data, and intentional inaccuracies are subject to penalties. This same review of studies found that the CPS data are a valuable source of information on the national low-income population, with broad and fairly accurate measures of income. However, the study noted that sample sizes might be small for some subpopulations (e.g., welfare recipients in particular states) and the percentage of some subpopulations covered by the survey appears to have declined modestly in recent years. The sample size for the targeted and nontargeted groups in our analysis was sufficiently large that the confidence intervals for the estimated employment rates were no more than 6 percentage points on either side of the estimate. We concluded that the slight decline in coverage of welfare recipients is unlikely to affect our analysis of trends in employment rates over the period.

As noted, we analyzed the tax data from IRS' Statistics of Income Division. These data undergo numerous quality checks but do not include information from amended tax returns (i.e., revisions made by taxpayers themselves after their initial filings).

# Appendix II: Survey Instruments

**GAO** U. S. General Accounting Office

## Survey of Work Opportunity Tax Credit (WOTC)-Related Employer Practices

### Program Participation Questions

#### Introduction

Congress has asked the U.S. General Accounting Office to review employers' use of the Work Opportunity Tax Credit (WOTC) program. As a part of the review, we are conducting a survey of employers in selected states who, like you, have hired workers under the program. We are interested in learning about your experiences, even if you have not claimed the tax credit.

The survey takes about 10 minutes to complete. Most of the questions in this survey can be answered by checking boxes or filling in blanks.

Information from the survey will not be used to assess your compliance with the law or to review your employees' eligibility for the program. We will not identify specific employers in our report. Before being included in our report, the information you provide will be combined with information provided by other employers. In addition, after completing our analysis, we will eliminate from our files the link between your company and the information you provide.

#### Instructions

This part of the survey should be completed by the person in your company who is most knowledgeable about your company's history with and implementation of the WOTC program. If another person in your company better fits that description, please forward the survey to him or her. Please consult with others in your company if assistance is needed to complete this survey.

Please return your completed survey within 14 days of receipt. You may return the survey by fax to Stuart Kaufman at (202) 512-4516, or if you wish, you may use the enclosed postage-paid envelope. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office  
Attn: WOTC Survey, Stuart Kaufman  
441 G Street, NW  
Room 2921  
Washington DC 20548

We urge you to complete this survey. We cannot develop meaningful information without your company's input. If you have any questions, please call Ms. Kerry Dunn at (415) 904-2234 or Mr. Kevin Daly at (202) 512-9040.

**Thank you very much for your time.**

Total sample size (unweighted) n=225  
Estimated population (weighted) N=1,838

NOTE: Percents reported are weighted percents based on the weighted N of 1,838. The number of employers (n, unweighted) who responded to the question is reported for each item. Percentages may not sum to 100% due to rounding, unless otherwise specified.

1. Who first raised the possibility of your company participating in the WOTC program? n=186  
(Check one.)

- 1.  Someone inside the company → *Continue with Question 2.* 57.2%
- 2.  Someone or some organization outside the company → *Skip to Question 3.* 24.5%
- 3.  I don't know → *Skip to Question 4.* 18.4%

2. What level of management or staff first raised the possibility of participating? n=109  
(Check one.)

- 1.  High level management in the company 76.6% \
- 2.  Another level of management in the company 20.5% >→ *Skip to Question 4.*
- 3.  Someone else - Please specify position: \_\_\_\_\_ 2.9% /

3. What type of organization or individual first raised the possibility of participating with your company? (Check one.) n=44

- 1.  A state or local governmental agency 24.4%
- 2.  A community-based organization 8.0%
- 3.  A trade association or local business organization 16.1%
- 4.  Other - Please specify: \_\_\_\_\_ 51.6%

4. We are interested in learning why your company decided to participate in the WOTC program. To what extent, if at all, did each of the following reasons influence your decision to participate in the program? (Check one box in each row.)

	To a very great extent (1)	To a great extent (2)	To some extent (3)	To little extent (4)	To no extent (5)	Not sure (6)
a. To obtain the tax credit n=186	66.3%	15.8%	10.4%	3.2%	1.3%	2.9%
b. As part of a strategy to address a labor shortage n=181	14.0%	20.2%	30.5%	13.8%	15.3%	6.3%
c. Positive past experience with target groups as good employees n=181	8.2%	14.8%	27.5%	14.5%	20.2%	14.9%
d. As part of a strategy to be a good corporate citizen n=184	16.1%	22.0%	36.3%	9.1%	9.3%	7.2%
e. Influence by other employers who are leaders in the industry or community n=181	3.8%	6.4%	11.2%	18.6%	46.9%	13.2%
f. Any other reasons? - Please specify: _____ _____ _____ n=15	54.9%	33.9%	11.2%	0%	0%	0%

5. Think about the types of positions for which you would consider hiring WOTC-eligible individuals. In the future, to what extent, if at all, do you think you will consider WOTC-eligible individuals when filling vacancies in these types of positions? (Check one.) n=221

- 1.  To a very great extent 33.8%
- 2.  To a great extent 37.3%
- 3.  To some extent 21.1%
- 4.  To little extent 3.4%
- 5.  To no extent 4.5%



6. To what extent, if at all, would each of the following reasons deter or discourage you from filling vacancies in these types of positions with WOTC-eligible individuals?  
(Check one box in each row.)

	To a very Great extent (1)	To a great extent (2)	To some extent (3)	To little extent (4)	To no extent (5)	Not sure (6)
a. Burdensome process n=184	9.3%	16.1%	26.6%	19.2%	28.1%	.7%
b. Desire not to be involved in a government program n=181	.8%	1.4%	8.5%	21.6%	67.2%	.5%
c. WOTC-eligible individuals are not good employees n=183	.8%	3.4%	10.4%	23.3%	58.7%	3.4%
d. WOTC is insufficient to offset costs n=181	2.7%	7.5%	17.9%	22.2%	47.8%	1.8%
e. Other hiring factors are more important than claiming the WOTC n=182	8.9%	20.8%	34.2%	10.4%	24.1%	1.6%
f. Any other reasons? - Please specify: _____ _____ n=10	64.6%	22.5%	13.0%	0%	0%	0%

7. Overall, how much do you estimate it costs your company to recruit, hire, and train each WOTC-eligible employee?

\$ \_\_\_\_\_ for the first year of employment n=118, mean=\$3,799

8. How much do you estimate it costs your company to recruit, hire, and train each non-WOTC-eligible employee in a similar position?

\$ \_\_\_\_\_ for the first year of employment n=117, mean=\$3,265

9. What percentage of your costs to recruit, hire, and train a WOTC-eligible employee would you estimate are covered by the WOTC?

\_\_\_\_\_ percent n=115 Mean=47.2%

10. When you think of effective employment practices, to what extent, if at all, do you think it is cost effective to terminate a current worker in order to hire a WOTC-eligible individual? (Check one.)  
n=219

- 1.  To a very great extent 1.0%
- 2.  To a great extent .7%
- 3.  To some extent 5.6%
- 4.  To little extent 9.9%
- 5.  To no extent 82.8%

11. When you think of effective employment practices, to what extent, if at all, do you think it is cost effective to terminate a WOTC-eligible worker whose earnings have reached the maximum eligible credit in order to hire a new WOTC-eligible worker? (Check one.) n=221

- 1.  To a very great extent 2.0%
- 2.  To a great extent 0%
- 3.  To some extent 5.0%
- 4.  To little extent 9.4%
- 5.  To no extent 83.6%

12. If you have any comments about the WOTC program, or about specific recruitment, hiring, training, or retention practices related to the WOTC, please enter them in the space provided. If you wish, you may add additional sheets.

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**Please return your completed survey by fax or using the enclosed envelope.  
Thank you so much for your help.**

**GAO** U. S. General Accounting Office

**Survey of Work Opportunity Tax Credit (WOTC)-Related Employer Practices**

**Employment Process Questions**

**Introduction**

Congress has asked the U.S. General Accounting Office to review employers' use of the Work Opportunity Tax Credit (WOTC) program. As a part of the review, we are conducting a survey of employers in selected states who, like you, have hired workers under the program. We are interested in learning about your experiences, even if you have not claimed the tax credit.

The survey takes about 10 minutes to complete. Most of the questions in this survey can be answered by checking boxes or filling in blanks.

Information from the survey will not be used to assess your compliance with the law or to review your employees' eligibility for the program. We will not identify specific employers in our report. Before being included in our report, the information you provide will be combined with information provided by other employers. In addition, after completing our analysis, we will eliminate from our files the link between your company and the information you provide.

**Instructions**

This part of the survey should be completed by the person who makes hiring decisions for your location. If more than one person makes hiring decisions for your location, the one who is most knowledgeable about WOTC-related employment practices in your company should complete the survey. If another person in your company better fits that description, please forward the survey to him or her. Please consult with others in your company if assistance is needed to complete this survey.

Please return your completed survey within 14 days of receipt. You may return the survey by fax to Stuart Kaufman at (202) 512-4516, or if you wish, you may use the enclosed postage-paid envelope. In the event the envelope is misplaced, the return address is:

U.S. General Accounting Office  
Attn: WOTC Survey, Stuart Kaufman  
441 G Street, NW  
Room 2921  
Washington DC 20548

We urge you to complete this survey. We cannot develop meaningful information without your company's input. If you have any questions, please call Ms. Kerry Dunn at (415) 904-2234 or Mr. Kevin Daly at (202) 512-9040.

**Thank you very much for your time.**

Total sample size (unweighted) n=225  
 Estimated population (weighted) N=1,838

NOTE: Percents reported are weighted percents based on the weighted N of 1,838. The number of employers (n, unweighted) who responded to the question is reported for each item. Percentages may not sum to 100% due to rounding, unless otherwise specified.

In the following questions, we will ask separately about some phases of the employment process: recruitment, hiring, training, and retention practices. If the process varies between locations in your company, please respond for your location.

1. Has your company changed its recruitment practices in any of the following ways to secure the WOTC for new hires? (Check one box in each row.)

	Yes (1)	No (2)
a. Entered a partnership with another organization to identify applicants n=211	33.8%	66.2%
b. Entered a partnership with another organization to screen applicants n=211	29.1%	70.9%
c. Entered a partnership with another organization to prepare people for employment n=210	12.9%	87.1%
d. Asked another organization to refer eligible individuals to your company n=212	42.6%	57.4%
e. Listed job openings with a public agency or partnership n=212	48.8%	51.2%
f. Changed wording in job listings n=209	5.0%	95.0%
g. Changed recruitment literature n=209	11.9%	88.1%
h. Set up a separate recruitment program to attract WOTC-eligible individuals n=208	12.1%	87.9%

2. Are there any other ways in which your company has changed its recruitment practices to secure the WOTC for new hires? (Check one.) n=212

1.  Yes → Please describe: \_\_\_\_\_  
 7.3%
2.  No 92.7%

3. Has your company changed its overall hiring practices in any of the following ways to secure the WOTC for new hires? (Check one box in each row.)

		Yes (1)	No (2)
a. Changed or modified the application packet	n=213	40.3%	59.7%
b. Trained managers about the tax credit	n=212	65.8%	34.2%
c. Offered managers incentives to hire WOTC-eligible individuals	n=211	20.7%	79.3%
d. Set up a separate process for WOTC hiring	n=212	20.0%	80.0%
e. Identified specific positions as appropriate for WOTC hiring	n=210	21.6%	78.4%
f. Changed or modified hiring standards	n=212	9.8%	90.2%
g. Hired a community-based organization or private company to conduct the hiring process	n=212	4.6%	95.4%
h. Hired consultants to process the certification paperwork	n=211	48.7%	51.3%

4. Are there any other ways in which your company has changed its overall hiring practices to secure the WOTC for new hires? (Check one.) n=212

1.  Yes → Please describe: \_\_\_\_\_  
4.0%
2.  No 96.0%

5. During the initial job interview, how much does the interviewer usually know about an applicant's eligibility for the WOTC program? (Check one box in each row.)

		Yes (1)	No (2)
a. Has the interviewer usually seen information, such as a state-issued conditional certification form, that indicates the applicant is likely to be WOTC-eligible?	n=173	26.0%	74.0%
b. Has the interviewer usually seen a completed WOTC screening form, such as IRS Form 8850 or DOL Form 9061?	n=172	37.9%	62.1%
c. Does the interviewer usually know that the applicant was referred by an agency as a member of a target group?	n=169	35.5%	64.5%
d. Does the applicant usually self-identify his or her own eligibility?	n=172	22.6%	77.4%
e. Does the interviewer usually ask about WOTC eligibility?	n=170	18.6%	81.4%
f. Does the interviewer usually guess about WOTC eligibility?	n=171	10.1%	89.9%
g. Does the interviewer usually prefer not to know about eligibility?	n=166	36.5%	63.5%

6. Does the possibility that an applicant may make your company eligible for the tax credit increase, decrease, or have no effect on the applicant's chance of being hired by your company?

(Check one.) n=212

- 1.  Increase greatly 10.9%
- 2.  Increase somewhat 31.3%
- 3.  Have no effect 57.2%
- 4.  Decrease somewhat 0%
- 5.  Decrease greatly .5%

7. Consider the vacancies your company has filled with WOTC-eligible individuals at your location. Of these vacancies, approximately what percentage falls into each of the following categories?

(Please enter percents. Your answers should add up to 100 percent.) n=108

	Mean %
a. Previous employee quit	61.1%
b. Previous employee was promoted	8.3%
c. Previous employee was transferred	2.8%
d. Previous employee was terminated for cause	11.6%
e. Position was newly created	11.8%
f. Other reason(s) vacancy occurred – Please specify: _____	4.0%

I don't know

8. In which of the following ways has your company changed its training practices to better prepare WOTC new hires for their positions? (Check one box in each row.)

		Yes (1)	No (2)
a. Provided basic work readiness training such as interaction with the public or proper work attire	n=208	38.0%	62.0%
b. Lengthened training times	n=207	33.2%	66.8%
c. Provided mentors or buddies within the company	n=206	39.9%	60.1%
d. Hired a community-based organization or private company to provide additional training or mentors	n=207	6.7%	93.3%
e. Set up a separate process to train WOTC hires	n=207	5.0%	95.0%
f. Changed or modified training materials	n=208	20.9%	79.1%

9. Are there any other ways in which your company has changed its training practices to better prepare WOTC new hires for their positions? (Check one.) n=210

- 1.  Yes → Please describe: \_\_\_\_\_  
5.5%
- 2.  No 94.5%

10. In calendar year 1999, how does the first year retention rate for WOTC-eligible employees at your location compare to the first year retention rate for non-WOTC-eligible employees in similar positions at your location? (Check one.) n=211

- 1.  WOTC retention rates are much higher 1.6%
- 2.  WOTC retention rates are somewhat higher 8.4%
- 3.  The rates are about the same 40.6%
- 4.  WOTC retention rates are somewhat lower 10.8%
- 5.  WOTC retention rates are much lower 3.5%
- 6.  I don't know 35.1%

11. Here is a list of potential problems companies sometimes have with their employees. For each of these potential problems, when you compare WOTC-eligible and non-WOTC-eligible employees in similar positions during the first month of employment, are the problems more prevalent, less prevalent, or equally prevalent among the two groups? (Check one box in each row.)

		Much more with WOTC (1)	Somewhat more with WOTC (2)	About the same (3)	Somewhat less with WOTC (4)	Much less with WOTC (5)	Not sure (6)
A. Absenteeism	n=169	6.9%	12.5%	46.9%	4.5%	5.0%	24.3%
B. Bad work attitude	n=169	3.8%	8.1%	46.3%	7.5%	8.1%	26.1%
C. Poor performance	n=169	6.1%	6.5%	51.3%	5.4%	4.4%	26.3%
D. Personal problems Interfering with work	n=169	8.6%	16.4%	40.1%	4.1%	2.7%	28.1%
E. Any other problems? Please specify:							
_____		46.2%	34.1%	19.7%	0%	0%	0%
_____	n=6						

12. In calendar year 1999, how does the voluntary separation (resignation) rate for WOTC-eligible employees at your location compare to the voluntary separation rate for non-WOTC-eligible employees in similar positions at your location? (Check one.) n=170

- 1.  WOTC voluntary separation rates are much higher 1.8%
- 2.  WOTC voluntary separation rates are somewhat higher 10.1%
- 3.  The rates are about the same 39.6%
- 4.  WOTC voluntary separation rates are somewhat lower 8.4%
- 5.  WOTC voluntary separation rates are much lower 3.4%
- 6.  I don't know 36.8%

13. You can provide information on the actual number of voluntary separations in calendar year 1999 for WOTC and non-WOTC employees in similar positions at your location, what is it?

WOTC ..... of \_\_\_\_\_ employees who separated, \_\_\_\_\_ voluntarily separated

Non-WOTC ..... of \_\_\_\_\_ employees who separated, \_\_\_\_\_ voluntarily separated

Information on actual voluntary separations is not readily available for: 1.  WOTC  
2.  Non-WOTC

[Results not reported for Question 13 because most respondents did not provide data]

14. When you think of the WOTC-eligible employees you have hired, how important is it to your company to retain such employees after the maximum credit has been secured? n=206 (Check one.)

- 1.  Very important 71.4%
- 2.  Somewhat important 20.0%
- 3.  Not very important 4.8%
- 4.  Not important at all 3.9%

15. If you have any comments about the WOTC program, or about specific recruitment, hiring, training, or retention practices related to the WOTC, please enter them in the space provided. If you wish, you may add additional sheets.

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**Please return your completed survey by fax or using the enclosed envelope.  
Thank you so much for your help.**

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# Appendix III: Statistical Analysis of State Databases

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To investigate whether reaching the maximum earnings in a given quarter affects the likelihood that employees will separate from their WOTC employers, we used state WOTC and unemployment insurance data on total earnings and duration of employment. We also used data from these sources on other employee characteristics, such as target group and occupation, and employer characteristics, such as total employment and the industry of the employer. The data were collected for 108,935 WOTC-certified employees and 5,347 employers in California and Texas for the years 1997 through 1999.<sup>1</sup>

We used the logistic regression model to quantify the effect of reaching the maximum earnings on the probability that the employee separates from the employer. We also used the model to estimate the effect of other employee characteristics, such as current wages (total earnings in a given quarter) and membership in a target group, on the probability of separation. The results of this analysis are presented as odds ratios in table 5. An odds ratio is a measure of relative risk of the occurrence of an event—in this case, the separation from an employer. The reported odds ratios indicate the effect of a particular characteristic (e.g., reaching the maximum earnings) on the probability of separation, controlling for the effects of other characteristics included in the analysis. The estimate of the effect, represented by the odds ratio, is the net effect of the characteristic (i.e., net of the effects of all other characteristics).

If the characteristic increases the probability of separation, the odds ratio will be greater than 1, and if it decreases the probability of separation, the odds ratio will be less than 1. This interpretation is slightly different when the characteristics are different categories. An example of such a “categorical” characteristic is membership in a target group where the categories are welfare recipients, veterans, food stamp youth, and so on. In such cases, the analysis omits one of the categories (called the “reference group”) and tests whether the included categories have greater

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<sup>1</sup>Using the WOTC databases provided to us by the states, we identified a total of 154,708 employees who were certified from 1997 through 1999 in California and Texas. We requested that the states match the social security numbers of these certified employees with the quarterly wage records in the states’ unemployment insurance databases. For both states, we found that nearly all the certified employees had wage records with some employer during the 12-quarter period. However, not all the employees had wage records with the employer identified in the WOTC database as the employer requesting the certification. A total of 108,935 certified employees were identified as working for the WOTC employer in the unemployment insurance database, indicating that 70 percent of certified workers had wage records that could be used for our analysis.

or less chance of separation relative to the omitted category. An odds ratio of greater than 1 indicates greater probability of separation, while an odds ratio of less than 1 indicates less probability of separation.

**Table 5: Logistic Regression Analysis of the Likelihood of Separation of Employees in California and Texas**

Variable name	Odds ratio
Current wages	0.92 <sup>a</sup>
<b>State</b>	
California	0.61 <sup>a</sup>
Texas	Reference group
Maximum earnings	1.01
<b>Target group</b>	
Welfare recipients	1.06 <sup>a</sup>
Veterans	1.29 <sup>a</sup>
Food stamp youth	Reference group
Employment zone/economic community youth	1.07 <sup>a</sup>
Ex-felons	1.54 <sup>a</sup>
Vocational rehabilitation	0.68 <sup>a</sup>
SSI recipients	0.84 <sup>a</sup>
<b>Interactions: target group and maximum earnings</b>	
Welfare recipients and maximum earnings	0.99
Veterans and maximum earnings	1.36
Employment zone/economic community youth and maximum earnings	1.17
Vocational rehabilitation and maximum earnings	1.19
Ex-felons and maximum earnings	1.56 <sup>a</sup>
SSI recipients and maximum	1.17
Food stamp youth and maximum	Reference group

<sup>a</sup>Indicates significance at the 5-percent level. Employees belonging to the summer youth target group were not included in this analysis. This target group has a different wage cap (\$3,000 of eligible first year wages), and members of the group are seasonal workers. The circumstances of their separations are therefore not comparable to those of members of other target groups.

Source: GAO analysis of California and Texas WOTC and Unemployment Insurance databases.

Table 5 shows that reaching the maximum earnings has no statistically significant effect on the odds that employees will separate from their employers. The variable called “maximum earnings” indicates the quarter in which an employee’s cumulative earnings are between \$5,000 and \$7,000. This interval includes \$6,000 as its midpoint and indicates that reaching the maximum occurs in the quarter when the employee is within \$1,000, more or less, of the maximum earnings eligible for the credit. The odds ratio for this variable is not significantly different from 1, meaning that employees whose earnings are within \$1,000 of the maximum in a

quarter are no more likely to separate than employees whose earning are outside this range. Table 5 shows that reaching the maximum has no effect on the likelihood of separation across most target groups as well. For example, members of the welfare target group are no more likely to separate in the quarter in which they reach the maximum than are members of other target groups who reach the maximum.<sup>2</sup>

We also used the logistic regression model to analyze the effect of reaching the maximum earnings separately for each state. The separate analysis permitted more characteristics of the employees and employers to be included because data on characteristics were not always available for both states. We analyzed the likelihood of separation in each state using only the characteristics in table 5, and then expanded the analysis to include the additional variable characteristics available in each state. This analysis shows that the conclusion about the effect of reaching the maximum on separation does not change when additional characteristics are added to the model. When variables indicating the occupation of the employee are added to the analysis in California, reaching the maximum earnings continues to have no effect on separation. When variables indicating the employer's industry and size in terms of total employment are added to the analysis in Texas, reaching maximum earnings is significant, but employees reaching the maximum are still slightly less likely to separate. Specifically, they are 9 percent less likely to separate than are employees who do not reach maximum earnings.

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<sup>2</sup>As table 5 shows, only members of the ex-felon target group had a statistically significant greater chance of separation when they reach the maximum earnings than members of other target groups when they reach the maximum. However, ex-felons represent only about 3 percent of all certified employees that we analyzed, and the results of the analysis for this group may not be as reliable as the results for other target groups.

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# Appendix IV: GAO Contacts and Staff Acknowledgments

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## GAO Contacts

Jim Wozny, (202) 512-9110  
Kevin Daly, (202) 512-9110

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