



STATE STRATEGIES FOR GROWING BUSINESSES AND CREATING JOBS

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ISSUE

Provide examples of state policies or programs generally cited as being effective in helping businesses grow and create jobs. Include tax policies designed to stimulate business growth.

SUMMARY

This report provides a general overview of state-level strategies for growing businesses and jobs, as well as some specific examples from states that have implemented these strategies. Generally, these strategies break into two categories: (1) general strategies that aim to improve the overall business climate, and (2) specific strategies that target businesses in certain sectors or in a particular stage of development. General strategies mainly provide tax and regulatory relief. Targeted strategies generally include financial assistance, tax incentives, technical assistance, and workforce development initiatives.

In addition to these traditional strategies, states are developing strategies that focus on innovation and the myriad factors that foster and sustain it. These holistic strategies aim to develop and coordinate policies and programs that address the "ecosystems" that allow businesses to start and thrive. Focusing on ecosystem models, such as innovation hubs and industry clusters, allows states to understand how elements of their regional economy fit together and tailor policy to foster innovation and grow industries.

We gathered the information for this report from different research publications on economic growth and job creation. Some examine and highlight specific state programs designed to grow business and jobs, and others present a synthesis of the common elements of similar programs from several states that researchers generally consider successful. In the interest of brevity, this report provides only a sampling of these programs and policies, not an exhaustive list.

It appears that states do not regularly and rigorously evaluate economic development policies and programs. Consequently, we could not find studies that extensively evaluated these policies and programs and identified those that have been successful in achieving their goals. Although many states measure policy and program outcomes (e.g., number of jobs created), few have tried to determine if they would have occurred without government assistance.

GENERAL STRATEGIES

Business Tax Relief

One often-discussed strategy for growing businesses and jobs is tax relief. [The National Governors Association's Center for Best Practices](#) (NGA Center) notes that the initial decision by a business about where to locate and the rate at which they grow is affected by taxes and suggests that states should consider their tax policy's impact on businesses as they craft state economic development policies. However, the NGA Center does not recommend specific actions, and policy analysts disagree over which tax policies are most effective for growing business and creating jobs.

Several national tax research organizations argue that tax relief measures are essential to spur business growth and create jobs. The [Tax Foundation](#) argues that taxes—particularly corporate and personal income taxes— inhibit economic growth and [favors](#) tax reform that reduces the overall tax burden and complexity. It believes that pro-growth tax reform broadens the tax base, lowers the tax rate, and eschews tax incentives, allowing the market to pick “winners and losers.” The Tax Foundation cites New York's 2014 [tax reform law](#) in New York as an example of pro-growth tax reform. The legislation: (1) gradually reduced from four to two the number of bases used to calculate the corporate income tax, (2) lowered the income tax rate from 7.1 percent to 6.5 percent, and (3) merged the duplicative bank tax system into the corporate tax system, among other things.

Although the Tax Foundation believes tax relief is an effective means of spurring business growth, other tax research organizations disagree. The [Center on Budget and Policy Priorities \(CBPP\)](#) [cites](#) numerous studies that found no correlation between taxes and economic growth. Rather than propose tax hikes, CBPP [contends](#) that state tax reform is not the appropriate policy avenue for spurring business and job growth because (1) state taxes are a very small expense for most corporations and (2) small businesses that expand do so because of product or service demand, not tax levels. Instead of spurring economic growth, CBPP believes that tax cuts could undermine it by reducing the revenue government needs to fund services businesses depend on (e.g., schools and roads).

Regulatory Relief

Although policy analysts disagree on effective tax policies for economic growth, they appear to agree that excessive regulation generally hinders business growth. The [NGA Center](#) notes that complicated regulatory environments are the biggest burden on businesses, especially small ones, and suggests that states should “assess whether permits, registration, and other bureaucratic requirements inhibit new business creation and take what measures are needed to change, simplify, and speed up the most burdensome government processes.” For example, New Jersey recently established a [Red Tape Review Group](#) to identify unnecessary regulation and passed a law, upon the group’s recommendation, to require the state to consider the economic impact of new regulations, prohibit rules that exceed federal standards, and streamline permitting processes.

The Kauffman Foundation (a nonprofit that funds research on entrepreneurship and education) suggests that states should focus on occupational licensing requirements and consider land-use reform to improve the overall regulatory environment and help new businesses succeed. The Foundation contends that although licensing is generally necessary, licensing requirements are often excessive and loosening restrictions could stimulate new entry without compromising quality of services. Although it does not provide a state model, it presents certification as an alternative to licensing, where a practitioner who meets certain standards receives a “right to title,” but non-certified people are allowed to practice. Regarding land-use reform, the Kauffman Foundation suggests that states allow local governments to permit mixed-use development, which attracts new businesses, and reduce local restrictions on home-based businesses.

Finally, some states have taken steps to make it easier for businesses to comply with regulations without necessarily reducing or eliminating regulatory requirements. A report by the National Conference of State Legislatures (NCSL) notes that Michigan and Virginia have created online “one stop centers” that provide all the information needed to start a business. Other states, such as Maine, have created small business advocates to guide business owners through the regulatory process. (In Connecticut, [PA 10-158](#) created a Permit Ombudsman and an expedited permitting process for certain projects that could help advance state economic development priorities.)

TARGETED STRATEGIES

Most policies and programs designed to grow business and create jobs are targeted to businesses in certain stages of development or certain key industry sectors. These policies and programs generally involve: (1) financial assistance, (2) tax incentives, (3) technical assistance, and (4) workforce development.

According to the [Kauffman Foundation](#), firms younger than five years create most of the new jobs each year. Therefore, many strategies target startups and the so-called “gazelles,” which are small, high-growth firms that make up about five percent of all businesses, but account for virtually all of net new job creation. In general, the NGA Center recommends focusing on businesses and industries already located in the state instead of recruiting those in other states. According to the center, although only two percent of annual job gains across states can be attributed to business relocation, many states have recently increased investments in strategic business attraction. The center notes that states generally use costly tax incentives and financial assistance packages to attract businesses to the state, and such programs may not provide the best return on investment.

Financial Assistance

Most states try to maximize the impact of their financial assistance programs by targeting funds to businesses and industries that have the highest potential to grow and create jobs. Common financial assistance strategies include (1) facilitating access to capital for startups and young, high-growth companies, and (2) targeting research and development grants to specific industries with a base in the state. (Connecticut Innovations, Inc. employs many of these strategies, but this report concentrates on examples from other states.)

Access to Capital. Most states encourage private investment in startups or “gazelles” through tax credits for individuals who invest in them (much like Connecticut’s [Angel Investment Tax Credit Program](#)). Many states also actively participate in venture capital investment either by (1) directly investing state dollars in startups or (2) by creating certified capital companies to leverage private investment (CAPCOs).

State direct investment programs generally target investment to specific industries that have high growth potential but are overlooked by venture capitalists. For example, some companies may perform well from an economic development perspective (e.g., creating jobs), but provide a lower financial return than private

venture capitalists desire. Despite state successes, direct investment programs have many detractors who believe that the risky nature of venture capital investment makes it an inappropriate use of state funds.

States also use insurance premium tax credits to fund investment by allocating such tax credits to CAPCOs, which then sell the tax credits to insurance companies and use the funds to invest in startups. According to the [NCSL](#), "insurance companies get tax credits on their investment (as kind of a substitute for interest rates), and they receive capital back at the end of the program, giving them an above average return with almost no risk." However, critics of CAPCOs believe these programs are costly for the state, heavily favor insurance companies, and lack transparency.

NCSL cites [MassVentures](#) as an example of a successful direct investment program. MassVentures, which was formed in 1978, provides seed and early-stage venture funding to high-growth startups as they develop new products and services for the market. The program claims the following successes: (1) 100% of its investment remained in Massachusetts, (2) companies in its portfolio have employed 7,500 individuals, and (3) 86% of funds were generated through gains in investing instead of government funding.

NCSL also cites Invest Maryland as an example of a successful hybrid state investment program. In keeping with the idea behind CAPCOs, Maryland auctioned off insurance tax credits in 2012 and used the \$84 million it raised to invest in startups in specific industries. Most of the investment funds are managed by private firms which committed to return, if successful, 100 percent of the principal and 80 percent of the profits to the general fund. The remaining funds are managed by the state-run Maryland Venture Fund.

Programs similar to the ones described above have existed for decades. However, an emerging approach for providing entrepreneurs with access to capital is equity crowdfunding. The concept is similar to that used by the website [Kickstarter](#), where individuals fund projects through an online platform and receive rewards for their pledges (for instance, a person could pledge money to his or her favorite musician's new album project in exchange for a copy of the completed album). Unlike rewards-based crowdfunding, equity crowdfunding allows individuals to buy small ownership stakes in a startup for a financial return. Although equity crowdfunding could open up new funding streams for entrepreneurs, it is largely uncharted territory for

policymakers and could present a number of challenges. For example, investment experts question whether consumers have the knowledge needed to make wise investments, and consumer protection advocates are concerned that scammers will masquerade as legitimate startups.

The Securities and Exchange Commission is working to finalize a rule change that would allow entrepreneurs to actively seek public investments and individuals to invest small amounts for a financial return. In the meantime, some states, including Georgia and Kansas, have developed [intrastate crowdfunding programs](#) to allow entrepreneurs within their state to seek investment from other state residents. In addition to allowing entrepreneurs to raise a certain amount of money by crowdfunding, many states have also set up websites to connect interested investors and startups.

Research and Development (R&D) Investment. Nearly every state has programs investing in R&D, generally targeting them to specific industries to maximize the investment's impact. R&D grants are awarded to firms, universities, and partnerships between the two, and are often used to leverage federal and private grants.

The NGA Center notes that most states target funding to fields most critical to the state's economic growth and support research projects with near-term commercial value that can be developed and realized locally. It also notes that most states use an intermediary organization (which generally include subject matter experts) to evaluate research proposals, monitor research investments, and stop funding if the research is not progressing as planned. Connecticut's Regenerative Medicine Research Fund, for example, provides grants to scientists who conduct research that shows clinical promise. The fund supports Connecticut's bioscience industry by supporting the fundamental research that is necessary for innovation but less likely to receive private funding.

Tax Incentives

According to the Pew Center for the States, states' use of tax incentives to encourage job creation and other business activities has increased substantially since the 1970s. Pew notes that every state has at least one tax incentive program (most have several), and the programs generally have different goals and structures tailored to the state's needs.

Pew recommends that states regularly and rigorously evaluate their programs to determine if they are meeting their goals and require policymakers to consider evaluations when deciding to continue a credit, but notes that none do so. In its

analysis, Pew determined that Connecticut was one of the ten states that are “leading the way” for tax incentive evaluation, but stated that it needs to better use such evaluations in the policy decision process and ensure that all incentives are properly evaluated.

To effectively evaluate tax incentives, Pew suggests that states: (1) establish a strategic and ongoing schedule to review all tax incentives, (2) ask and answer the right questions with good data, (3) determine whether tax incentives are achieving the state’s goals, and (4) build evaluations into policy and budget deliberations to ensure that lawmakers use the results. Pew also notes that good evaluations answer these questions:

1. Did tax incentives change business decisions, and how much would have happened anyway? (cause and effect)
2. To what extent did the incentive benefit some businesses at the expense of others? (winners and losers)
3. How much of the benefit flowed across state borders? (unintended beneficiaries)
4. How long will the benefits last? (timing)
5. To what extent do the investments of companies filter into the broader economy? (indirect impact)

Technical Assistance

Businesses need more than funding to succeed, and state technical assistance programs provide businesses with the various kinds of support (e.g., access to commercialization experts) they need to grow and create jobs. In this section, we focus on three models that support entrepreneurs and specific industries: entrepreneurial networks, accelerators, and industry-specific centers and services.

Although entrepreneurs often believe their success hinges on funding, the Kauffman Foundation cites a growing body of evidence demonstrating that an entrepreneur’s access to other entrepreneurs, potential employees, potential funders, and service providers (networks) is the most important factor in determining his or her future success. Consequently, many states have taken steps to develop these critical networks. NCSL highlights Indiana’s Elevate Ventures program, which provides entrepreneurs with advisory and technical assistance in all aspects of business, including obtaining federal grants and identifying potential investors. Some entrepreneur networks, such as Virginia’s Entrepreneur Express, also coordinate workshops and training opportunities for entrepreneurs.

Several states have also created formal technology accelerators to quickly grow companies with potential. Often confused with incubators, which provide space and general support services for startup businesses in the early stages, accelerators are short, competitive, and intense programs that provide specialized support, including funding in exchange for equity, to businesses in the “adolescent” phase.

Accelerators are generally focused on specific industries and are highly selective—only a few companies with the highest potential are selected to participate. Among other things, accelerators provide mentors, access to funding networks, and technical assistance with business planning and proof of concept. The State Science and Technology Institute (SSTI) highlights the NEXUS-NY clean energy accelerator, which provides researchers with a year-long immersive learning course in startup techniques and connects participants with mentors and experts in technology and business development. Successful accelerator programs are tied to the state’s industry strengths, and are particularly helpful in commercializing research.

Many states also have programs to support established businesses in targeted industries. Several states, including Connecticut, have built science and technology centers to support and connect businesses within industries. In addition to providing industry-specific facilities and training, these centers facilitate university-industry collaboration. Although most industry-specific training programs have a technology focus, others aim to grow small industries that show potential. For instance, North Carolina has devoted resources to assist its cluster of furniture companies in increasing furniture exports, including providing market research for the entire sector and coordinating trips to trade shows.

Education and Workforce Development

According to NCSL, the shift from an industrial-based economy to one that is knowledge-based has made workforce development and education a critical component of economic growth. Education can give entrepreneurs the knowledge and encouragement needed to start new businesses, and rapidly growing industries—such as advanced manufacturing—need an increasing number of skilled workers to continue to meet increasing demand for products and services. States seek to increase entrepreneurship and support rapidly-growing industries through different education and workforce development initiatives, including: (1) experiential entrepreneurship programs, (2) industry-university alignment incentives, and (3) middle-skills job certificates and training.

In order to increase the number of startups, several studies recommend that states promote entrepreneurship as a viable career option. To do this, the Kauffman Foundation recommends promoting and encouraging experiential entrepreneurship programs at universities and community colleges. Rather than provide traditional

college courses in entrepreneurship, these programs teach students to be entrepreneurs by having them start actual companies and learn as they go. Participating students receive a mentor and other necessary support, but unlike traditional business incubators and accelerators, these programs have little or no fees (other than tuition, in some cases) and take zero equity in students' companies. An example of a successful program is Stanford University's StartX, which has produced 190 companies (70% of which are still funded and growing), several of which have been acquired by companies like Apple, Yahoo, and Dropbox.

To support their targeted industries, many states have crafted policies that align postsecondary education with industry needs. The NGA Center noted that recent fiscal struggles have shifted state strategy from increasing overall investment in postsecondary education to finding ways to use existing funding to encourage colleges to meet state goals. Several states have transitioned to performance-based funding that rewards educational institutions for outputs (e.g., degrees awarded) instead of inputs (e.g., enrollments). New Mexico recently allocated five percent of total university funding for performance-based funding, and the formula it uses to allocate performance-based funding includes the number of degrees completed in state workforce priority areas.

Another significant challenge for high-growth industries is finding people qualified for middle-skills jobs (or jobs that require a certificate or associate's degree). According to the Georgetown Center on Education and the Workforce, by 2020 35% of jobs will require a bachelor's degree, but a nearly equal number (30%) will require a certificate or associate's degree. The Oregon Career Pathways Initiative seeks to develop the state's future workforce by working with community colleges to ease the transition from high school to college and increase the number of residents with certificates or associate's degrees. This is part of Oregon's broader 40-40-20 Goal, which states that by 2025, 40% of the workforce will have bachelor's degrees or higher, 40% will have a certificate or associate's degree, and 20% will hold a high school diploma. Oregon also created Career Pathway Certificates of Completion (CPCC), which are flexible, short-term certificates that qualify students for an entry-level job.

CREATING REGIONAL "ECOSYSTEMS"

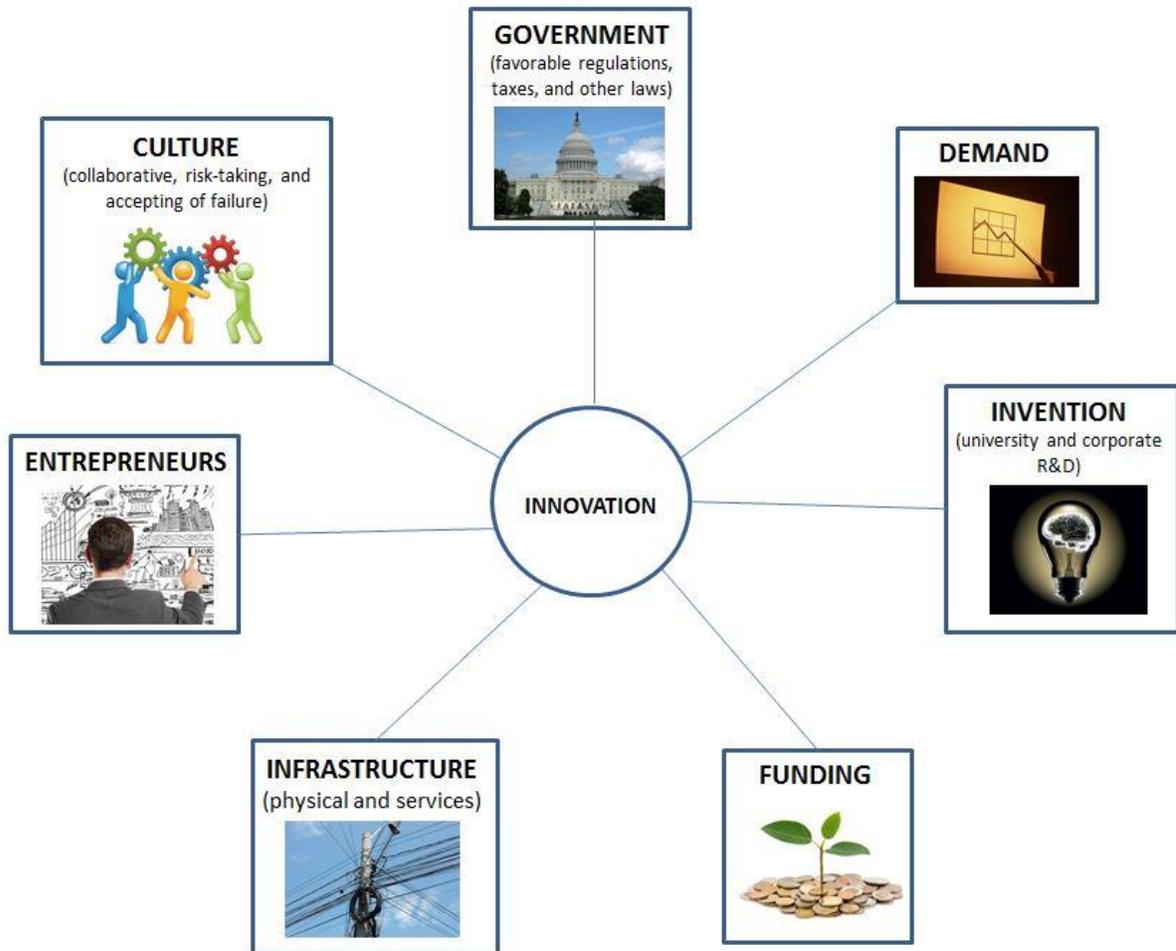
Over the past few decades, many economic and policy researchers have looked beyond tax and regulatory relief and programs tailored to individual business needs to the host of factors that explain why some businesses grow and thrive. These factors comprise local and regional ecosystems, and the NGA center notes that states can have the greatest impact on the regional economy by creating and coordinating policies that allow these ecosystems to thrive.

Innovation hubs and industry clusters are two models developed by researchers that can help lawmakers understand these systems, identify needs, and combine individual policies and programs (including many of those discussed in this report) to maximize the impact on the local and regional economies. Innovation hubs focus on innovation and entrepreneurial activity within a region (but not necessarily in a specific industry) and on the connections between the individuals and organizations that help drive the innovation process. Industry clusters focus on supporting related companies (in all stages of development) and allied institutions, such as universities, located within a region. At the core of these models is the understanding that each region's strengths and needs are different. Therefore, rather than providing a specific set of policy initiatives, these models help states assess regional needs and determine how to adapt policies and programs to meet those needs. Several states have successfully developed policies to support innovation hubs and industry clusters. In doing so, they provide a method for analyzing an economy, identifying its unique strengths and weaknesses, and crafting policies and programs based on that analysis.

According to the NGA Center, an innovation hub is an "ecosystem in which a distinctive collection of people, firms, institutions, and relationships combine in finely tuned ways to not only provide scientific advances or technological breakthroughs, but to also turn ideas into products and take them rapidly to market by creating new firms." William Aulet, an entrepreneurship researcher at the Massachusetts Institute of Technology, describes this idea more simply, presenting innovation as an equation: $\text{innovation} = \text{invention} + \text{commercialization}$. He notes that successful innovation hubs consist of seven elements (shown in figure one) that work together to accelerate the innovation process. Each of these elements is necessary, but none are sufficient on their own.

Innovation Hubs

Figure 1. Elements of an Innovation Hub



Source: NGA Center

Aulet emphasizes that all seven elements of the hub must be present for innovation to thrive within a region. But his research has found that, of the seven elements, two elements—culture and entrepreneurs—seem to have the greatest impact on regional innovation. Given this, he suggests that states can help strengthen an innovation hub by crafting policies and programs that attract and support entrepreneurs in the region and foster a culture of innovation that encourages risk-taking. Aulet identifies culture as the most significant element of an innovation hub and notes that a successful innovation culture: (1) celebrates the entrepreneurial spirit and holds entrepreneurs in high esteem for taking a chance, (2) treats failure as part of the innovation process, (3) creates visible entrepreneurial role models who are the proverbial “rock stars,” and (4) encourages young people to become

entrepreneurs, rather than promoting “safe” jobs with established companies. Aulet says states can cultivate this culture and support entrepreneurs by giving entrepreneurs visibility with focused events, workshops, and competitions. Praising and rewarding (both financially and ceremoniously) the entrepreneurial spirit encourages budding entrepreneurs to pursue their ideas and presents entrepreneurship as a worthwhile and admirable career path.

Industry Clusters

Every state economy has clusters, which the NGA Center describes as “geographic concentrations of similar and related firms, their workers, and supporting institutions.” Clusters drive business success by attracting concentrations of skilled workers and supplier industries and fostering inter firm collaboration that advances industry knowledge and innovation, among other things. The NGA Center also notes that recent data shows that strong clusters accelerate job growth, pay higher wages, and promote entrepreneurship. Focusing on industry clusters helps states scale up from supporting individual companies to creating systems that help many companies become competitive, thereby attracting and retaining businesses in a region and maximizing the impact of state funds.

To effectively grow industry clusters, states must first identify and understand each cluster’s strengths and weaknesses. The NGA Center notes that states should be realistic in their efforts, focusing on strengths that already exist rather than trying to create something new. After identifying clusters, states can work with cluster leaders to craft policies that address the cluster’s strategic needs. Because each cluster faces different challenges, a one-size-fits-all policy will not be effective. The NGA Center presents a few specific approaches that can be adapted for each cluster, including: (1) convening, or bringing the right public and private actors together to strategize, (2) funding education and workforce training, (3) investing in research and incentivizing private actors to do the same, and (4) purchasing local goods and services. It also notes that state leaders who are knowledgeable about industry clusters can use public forums to show they are serious about growing industry sectors, which helps give confidence to private investors and attract talent to the region. As with innovation hubs, the most important aspect of cluster-based strategies is that policies be designed to work together to maximize impact.

The NGA Center cites The California Institute for Quantitative Biosciences (QB3) as an example of a successful cluster initiative. Created in 2000 to support California’s bioscience cluster, QB3 provides services to companies within the bioscience industry, including helping firms find experts or research facilities with advanced equipment. It also organizes and facilitates research collaborations between

university researchers and companies, in part by helping to simplify the complicated bureaucratic process required to create a formal research partnership between a business and a university. QB3 also supports several incubators that provide startup bioscience companies with support services and laboratory space.

HYPERLINKS

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