



## Economic Impact Group, LLC

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### Estimating the Economic Impact of REI's New Market Tax Credit Investments, 2003 – 2007

Prepared By:  
Economic Impact Group, LLC  
17912 Barrington Drive  
Edmond, OK 73003

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## **Introduction**

Rural Enterprises of Oklahoma, Incorporated (REI) recently celebrated 25 years of fostering economic development projects in the state of Oklahoma. The staff at REI oversees diverse development services ranging from administering a variety of USDA and U.S. SBA loan programs to providing business incubators for infant enterprises to offering technical and administrative support through their Women's Business Center. A relatively recent addition to their array of development offerings arises in the participation in federal and state tax credit programs. Though new, these programs comprise an increasing share of REI's overall activities and contribute substantially to the broader economic impacts resulting from their efforts.

Economic Impact Group, LLC is a private consulting firm located in Oklahoma City specializing in impact and policy analysis and has been retained by REI to estimate the broader economic impacts of projects financed through REI's participation in federal and state tax credit programs. All data used in the impact estimation has been provided by REI senior staff, who assume sole responsibility for the accuracy of reporting. The economists at EIG analyzed, prepared, and input the data into an appropriate impact model and are solely responsible for any errors involved in the estimation of economic impacts.

Impacts from REI's participation in federal and state tax credit programs on Oklahoma production, employment, and labor income are estimated using Implan (Impact Analysis for PLANning) modeling software. Implan was developed by the USDA Forest Service in conjunction with the University of Minnesota as a relatively low cost method of analyzing the broader economic impacts of regional projects. Implan is currently maintained and marketed by the Minnesota Implan Group and is commonly employed in both private and public sector analysis.<sup>1</sup>

The economic models that serve as the foundation for the Implan software are characterized by restrictive assumptions about the regional economy under study. Specifically, the methodology starts with a snapshot of the economy, and using the structure reflected by this initial economic snapshot estimates the changes to economic outcomes resulting from the introduction of some new economic activity. In the context of this report, Implan essentially compares economic outcomes in the case with REI financed projects in the economy versus without REI financed projects in the economy. The difference of these cases, then, provides a way to estimate the impact of REI financed projects on Oklahoma production, employment, and income. Economic impact models are not forecasts of actual economic outcomes and should not be used as such. They do, however, provide valuable information concerning the effectiveness of development projects in creating additional economic activity, jobs, and income. All impact results presented in this report should be viewed in this context.

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<sup>1</sup> For more information, go to [www.implan.com](http://www.implan.com).

## **Summary of Results**

Through their recognition as a Community Development Entity by the U.S. Treasury's Community Business Administration REI is effectively able to leverage large sums of financial capital into Oklahoma development projects. As the initial economic impact and secondary economic impacts ripple through the economy, the aggregate impact can often far exceed the initial expenditure. A review of REI's tax credit data and resulting model output reveal the following highlights.

- REI participates in projects in which they just one of several investors. By injecting additional investment capital into the development process, REI allows private investors who may or may not be utilizing tax credit programs to spread their investment capital across more projects, thereby offering outside investors a more diverse portfolio of venture investments. REI's participation alone serves to attract a higher level of investment activity than is likely to occur otherwise.<sup>2</sup>
- The data used in the subsequent estimation involve 30 distinct projects (a few of which involve the same organization pursuing different projects).
- The raw data provided by REI indicate they have successfully leveraged over \$208 million into development projects.
- Financing used to purchase a business's existing assets (land, structure, inventory, etc.) contribute relatively little to changes in new demand, which are typically limited to real estate, legal, and other transactions fees. The real impact from these projects is realized through the ongoing operations of the enterprise. These impacts are not included in the analysis as sufficient information is not available. This implies that the impact estimates reported are likely very conservative estimates.
- Of the \$208 million invested, just over \$138 million is included in the analysis. The remainder was used to purchase existing assets with the subsequent impacts realized through ongoing operations and not included in this report.
- The aggregate impact of projects funded the federal tax credit programs is estimated to be an additional \$163,499,728 in Oklahoma produced goods and services, creating 1562.8 new jobs and \$58353774 in labor income.
- The aggregate impact of projects funded through state tax credit programs is estimated to be an additional \$91,004,765 in Oklahoma produced goods and services, creating 915.8 new jobs and \$32,120,088 in labor income.
- The combined aggregate impacts from both federal and state tax credit programs is estimated to be an additional \$254,504,486 in Oklahoma production, creating 2478.6 new jobs and \$90,473,862 in labor income.<sup>3</sup>

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<sup>2</sup> All impact figures are estimated using REI's portion of the project only. Estimating the impact of the entire value of the project would necessarily increase the impact estimates reported. However, since it is impossible to identify the exact quantity of additional capital brought to the process through REI's participation, we opt for a more conservative estimate of the resulting economic impacts.

<sup>3</sup> All impact figures are reported in current dollar values to facilitate comparisons.

- On average, every \$1 million invested by REI increases Oklahoma production by \$1.84 million, suggesting that in addition to the \$1 million of REI direct investment, an additional increase of \$844,000 in Oklahoma production is brought about by the multiplier effect.
- On average, every \$1 million invested by REI increases Oklahoma income by just over \$655,000 and created just over 18 new jobs.<sup>4</sup>
- On average, every \$1 million invested by REI increases Oklahoma production by \$1.84 million while creating 18 new jobs with an average annual salary of \$36,400.

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<sup>4</sup> The jobs created number is estimated according to the “snapshot” of the economy used in the analysis, as are all estimates. It certainly understates the importance of the programs to the workforce, as it ignores the reality of jobs retained through financing. For REI’s in-house estimate of jobs affected (retained plus created) go to [www.ruralenterprises.com](http://www.ruralenterprises.com).

## **Study Overview and Methodology**

The purpose of this study is to assess the broader economic impacts stemming from the execution of projects financed through federal and state tax credit programs administered by Rural Enterprises of Oklahoma, Incorporated. In estimating the economic impacts of the development projects financed through these systems, we begin first by defining the relevant economy of interest and the process by which capital injections work their way through the economy.

The current report takes the state of Oklahoma as the economy of interest and seeks to identify specifically the impact of REI funded projects on Oklahoma production, jobs, and labor income. An economy can be thought of as a system by which fundamental institutions inherent to all economies are connected and through which they interact. The three fundamental institutions are households, firms, and governments, and can be thought of as being interconnected by a pipeline through which resources and commodities flow. Resources such as physical and financial capital and labor services flow from households to firms. In return, goods and services flow from firms to households. Governments tax both resource and commodity flows, as well as consume goods and services and redistribute income.<sup>5</sup> Impact analysis begins by injecting this system with an infusion of new spending and observing the system after it has fully adjusted.

Impact estimates are not economic forecasts. Impact analysis looks at a snapshot of the economy described above taken at a given point in time and uses the resulting picture to replicate the structure of the economy. In doing so, it holds constant all relevant relationships in the economy such as consumer spending patterns, firm production patterns, and government tax and spending patterns. We then inject new spending, or new final demand, into the economy, and consistent with the structure provided by the snapshot observe the resulting changes to production, income, and employment. For illustration purposes, suppose we wish to estimate the impact of a \$10 million construction project. We inject \$10 million in new construction spending and observe in our system that doing so causes the construction industry to purchase new inputs (equipment, materials, labor, etc.) as they work to complete the original project. Each of these supporting industries (wholesale building suppliers, for example) must purchase additional inputs (materials and labor) as they strive to meet the increased demand for their services resulting from the original construction project. At each stage, additional labor is being hired and additional labor income is being spent in accordance with the household consumption pattern captured by our snapshot of the economy. The aggregate impact (original change in new demand plus change in new demand from supporting industries plus change in new demand by household consumption) can far exceed the size of the original project and is referred to as the multiplier effect.

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<sup>5</sup> A fourth institution can be thought of as all institutions outside the defined economy of interest and characterized as “the rest of the world.”

### **Federal Tax Credits**

In April of 2002, REI New Markets Investment, LLC was formed as a wholly owned, for profit subsidiary of REI. It is through this subsidiary that REI administers both federal and state tax credit programs.

The federal New Markets Tax Credit program was established as part of the Community Renewal Tax Relief Act of 2000. Under the program, investors receive a credit against Federal income taxes for making qualified equity investments in a designated Community Development Entity. Substantially all of the investment must be used by the CDE to make investments in low-income communities. The investor, in turn, receives a credit of 39% of the total investment taken over a 7-year period.<sup>6</sup> To date the CDFI fund has made 294 awards nationally totaling \$16 billion in allocation authority and is preparing to award an additional \$3.5 billion in allocation authority.

Table 1 below, gives the aggregate impact to Oklahoma production, employment, and earnings resulting from projects funded through REI's administration of the Federal New Markets Tax Credit program.

**Table 1**  
**Federal New Markets Tax Credits: Output, Employment, and Earnings Impacts**

<b>Year</b>	<b>Output</b>	<b>Employment</b>	<b>Earnings</b>
2003	2,265,751	22.4	741,538
2004	79,853,352	713.4	27,767,356
2005	18,640,824	203.4	7,121,529
2006	13,750,976	94.4	4,098,780
2007	50,620,981	538.9	19,048,537
<b>TOTAL</b>	<b>163,499,728</b>	<b>1562.8</b>	<b>58,353,774</b>

The impact reports are estimates of the long run influence of the projects closed during the specified year and do imply that the full economic impact is felt by the economy during that calendar year. For example, the projects closed under this program during 2004 have an estimated impact of a \$79,853,352 increase in Oklahoma production of goods and services. The impacts of the 2004 projects likely continue to reverberate through the economy, and hence, the economy continues to feel the impacts of these projects many years later.

Table 1 immediately reveals the success of the program in attracting large sums of investment capital into otherwise underserved areas. The aggregate impacts from the projects funded through federal tax credit programs include a nearly \$163.5 million increase in Oklahoma output, over 1560 new jobs, and over \$58 million in earnings. It must be noted that these impacts are quite conservative in nature. Data permitting,

<sup>6</sup> The 39% credit is distributed as a 5% credit in each of the first three years and 6% credit taken annually in each of the four remaining years. For more information on the New Markets Tax Credit program, go to [www.cdfifund.gov](http://www.cdfifund.gov).

impact analysis should include impacts from the ongoing operation of the new businesses created through these projects. Because this data is not available, the reported results indicated the expected impacts from the initial projects only. Also, a significant portion of the funds supplied have been used to acquire existing businesses (structures and assets). The acquisition of an existing enterprise contributes only a fraction of the initial transaction to new production (usually limited to real estate, legal, and financial fees). The lion's share of the impact from such an acquisition is only realized through the operation of the enterprise and, again, is omitted from the current analysis.

**State Tax Credits**

The Oklahoma Small Business Capital Formation Incentive Acts are among several economic development tools employed by the state. Under the provisions of the act, a share of the investment in a qualifying small business or Small Business Capital Investment Fund can be applied as a tax credit toward any number of designated state tax liabilities. The share of investment that can be claimed varies by location, with 30% qualifying for rural investment and 20% for urban investment.

Table 2 below gives the aggregate impacts on Oklahoma production, employment and earnings resulting from projects funded through state tax credit programs. Again, all impact figures are long-run impact estimates. Thus, the 2003 impacts are correctly interpreted as the impacts likely to result from projects closed in 2003 and not as impacts realized in 2003. In fact, it is likely that positive economic impacts from these projects continue to ripple through the economy many years later.

**Table 2**  
**State Tax Credit Program: Output, Employment, and Earnings Impacts**

<b>Year</b>	<b>Output</b>	<b>Employment</b>	<b>Earnings</b>
2004	763,691	7.5	281,815
2005	43,324,966	509.6	17,287,956
2007	46,916,108	398.7	14,550,318
<b>TOTAL</b>	<b>91,004,765</b>	<b>915.8</b>	<b>32,120,088</b>

Table 2 highlights the successful use of state tax credit programs to contribute just over \$91 million to Oklahoma production while creating 915 jobs and over \$32 million in labor earnings. Again, these estimates do not include the continuing impacts from the ongoing operations of the enterprises created or expanded through these programs.

## Conclusion

The projects funded through federal and state tax credit programs have had a profound and undeniable impact on the Oklahoma economy. The estimates provided are impressive in spite of their conservative nature – they include in analysis only the REI portion of the project when multiple investors are present in a single project, they do not include impacts from ongoing operations, and they include only a fraction of the investment indicated as being used for real estate or asset acquisition.

The impacts from the projects funded through tax credit programs are spread across Oklahoma industries and communities. Table 3 below combines the state and federal programs to estimate the impacts to output, employment, and earnings within major industry classifications in Oklahoma. The relatively large impacts enjoyed by the construction and manufacturing industries are largely the result of projects whose primary use was to purchase Oklahoma construction services and manufacturing output. The secondary effects are highlighted by the impacts enjoyed broadly across Oklahoma's diverse industries.

**Table 3**  
**Federal and State Tax Credit Programs: Combined Industry Impacts**

<b>Category</b>	<b>Output Impact</b>	<b>Earnings Impact</b>	<b>Employment Impact</b>
Agriculture, forestry, fishing and hunting	1,389,268	293,151	16.5
Mining	3,985,123	851,191	9.4
Utilities	3,153,676	626,719	4.4
Construction	77,852,024	35,340,540	1,044.3
Manufacturing	45,952,564	10,620,978	158.1
Wholesale Trade	20,153,264	7,573,799	142.2
Retail Trade	12,352,319	4,766,656	193.2
Transportation and Warehousing	4,779,793	1,886,133	41.3
Information	5,481,855	1,069,984	21.7
Finance and insurance	7,631,893	2,143,489	51.4
Real estate and rental and leasing	6,321,197	1,235,572	56.6
Professional, scientific, and technical services	27,025,928	11,219,919	245.6
Management of companies and enterprises	1,993,269	863,958	11.0
Administrative and waste management services	5,622,280	2,616,896	121.4
Educational services	734,157	358,731	15.1
Health care and social assistance	9,761,699	5,013,441	123.2
Arts, entertainment, and recreation	871,320	318,822	22.1
Accommodation and food services	4,430,071	1,363,464	94.8
Other services	5,067,298	1,892,876	96.7
Government and non-NAICS Institutions	7,922,789	417,545	9.7
	2,022,701	0	0.0
<b>TOTAL</b>	<b>254,504,486</b>	<b>90,473,862</b>	<b>2,478.6</b>

Rural Enterprises of Oklahoma, Inc. is a multi-faceted development organization with a 25-year history of facilitating economic growth in Oklahoma. The relatively recent addition of their New Markets Investment subsidiary allows them to complement their other services by providing financing for relatively large projects through federal and state tax credit programs. REI's positive reputation and existing infrastructure facilitates their success in these programs. The current analysis estimates the impacts on the Oklahoma economy from just over \$208 million of REI funded investments and finds a resulting impact of almost \$255 million to Oklahoma production of goods and services, over \$90 million in labor earnings, and the creation of 2,478 new jobs.