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Key Findings and Recommendations
Overview

The Technology Transfer Income Tax Exemption was created in 1987. For tax years starting on or after January 1, 1988, it allows corporations to exempt from income 10 percent of gross proceeds from the transfer of technology to an Oklahoma small business for 10 years. While not specified in statute, the goals of the program are likely to provide support for the transfer of technology to Oklahoma small businesses that do not have the resources to produce technology that may provide operational efficiencies or provide innovative products to the market.

Based on the characteristics of the program and the lack of comparable programs in other states, it is unclear if this program is addressing a critical need for the State's economy. Many states make an effort to support technology transfers, but use methods that benefit small businesses directly. Many states also concentrate efforts to support technology transfer on public research universities where technology is developed. Due to a lack of data regarding the usage and cost of the tax exemption offered by the program, it is also unclear how oft-used the program is, which could be one indication of the need for this incentive.

Overall Recommendation: Based on the lack of comparable programs, and lack of data available to estimate its cost and benefit, the project team recommends reconfiguring the program by requiring additional data to be collected and evaluated prior to determining whether to retain or repeal the program.

Key Findings Related to Established Criteria for Evaluation

The Oklahoma Tax Commission (OTC) is unable to provide data on the use of the exemption. Corporate tax exemptions are reported as part of the calculation of Oklahoma taxable income for corporate income tax returns as part of Form 512. The OTC collects this information in order to review it in the case of an audit, but it does not process this information at an aggregate level for the determination of the total cost of the corporate income tax exemption. As a result, the OTC has not provided an estimate of the cost of this exemption, the number of returns claiming the exemption, or the trends in its usage over time. Without this data, it is not possible to determine the usage, fiscal impact, or economic impact of the program.

Other states seeking to support small business technology transfers use different methods. Arkansas has a program that offers grant funding in order to reduce transfer transaction costs. Many other states have programs that supplement the federal Small Business Technology Transfer program through technical training, funding of the application process, or grant funding matching federal funds.

Changes to Improve Future Evaluations

The following information should be collected by OTC in the future to improve evaluation of the program's impact:

- Amount of tax exemptions per year
- Number of tax exemptions per year
- Amount of gross proceeds from technology transfer associated with the exemption
- North American Industry Classification System (NAICS) codes associated with transferors and transferees
- Description of the technology being transferred
Introduction
Incentive Evaluation Commission Process Overview

In 2015, HB2182 established the Oklahoma Incentive Evaluation Commission (the Commission). It requires the Commission to conduct evaluations of all qualified state incentives over a four-year timeframe. The law also provides that criteria specific to each incentive be used for the evaluation. The first set of 11 evaluations were conducted in 2016, and an additional 12 were conducted in 2017.

The Technology Transfer Income Tax Exemption is one of 11 incentives scheduled for review by the Commission in 2018. Based on this evaluation and their collective judgment, the Commission will make recommendations to the Governor and the State Legislature related to this incentive.

Technology Transfer Income Tax Exemption Incentive Background

The Technology Transfer Income Tax Exemption was created in 1987. For tax years starting on or after January 1, 1988, it allows corporations to exempt from income 10 percent of gross proceeds from the transfer of technology to an Oklahoma small business for 10 years.

Small businesses often do not have the resources to perform research and development activities in order to improve operational efficiency or create new products. Technology is often transferred to commercial businesses from research institutions. While research institutions are well equipped to perform the scientific research and development activities necessary to create new technology, they often lack the ability and resources to commercialize a product. As a result, the transfer of technology to commercial entities is often a critical step toward creating and marketing new technology.

Criteria for Evaluation

A key factor in evaluating the effectiveness of incentive programs is to determine whether they are meeting the stated goals as established in state statute or legislation. In the case of this program, its goals are not clearly stated in statute. However, based on the characteristics of the program, the intent appears to be to support the transfer of technology to businesses in Oklahoma that may not have the resources to perform research and development activities.

To assist in a determination of program effectiveness, the Incentive Evaluation Commission has adopted the following criteria:

- Comparison of Oklahoma incentive to other states
- Number and amount of technology transfers
- Dollar value of benefit
- Employment and payroll associated with the technology transfer

The criteria focus on what are generally considered key goals of incentive programs – in this case, for example, employment and payroll associated with the technology transfer incented by this program. Ultimately, incentive programs have to weigh both the benefits (outcomes related to achieving policy goals and objectives) and the costs, and that is also a criterion for evaluation (State return on investment). These will be discussed throughout the balance of the evaluation.
Incentive Usage and Administration
Program Administration

The Technology Transfer Income Tax Exemption is administered by the OTC. In order to claim the exemption, the OTC requires corporations to list the amount of exemption claimed on Form 512 in part 1 or 2, where Oklahoma taxable income is calculated.

The exemption allows corporations to exclude from taxable income a portion of royalty payments received as a result of a transfer of technology to a small business in Oklahoma. The corporation may exclude 10 percent of the gross proceeds from this transfer per year for up to 10 years.

To qualify for the exemption, the recipient of the transferred technology must be a business organized for profit in Oklahoma with capitalization of no more than $250,000 and with at least 50 percent of its employees and assets located in the State. Statute prohibits the use of this exemption by subsidiaries or affiliates of the corporation making the transfer. The qualifying transferred technology may be a proprietary process, formula, pattern, device or compilation of scientific or technical information that is not in the public domain.

Use of the Program

Although the OTC requires taxpayers to claim the exemption on Form 512 and list the amount of the exemption claimed, this data is not processed by the OTC. The OTC collects this information on corporate income tax for review for case-by-case audits, but it does not aggregate this for the determination of the total cost of any corporate income tax exemption. Therefore, the OTC is unable to provide any estimate of the cost of this exemption, the number of returns claiming the exemption, or the trends in its usage over time. Without this data, it is not possible to determine the use of the program.
Economic and Fiscal Impact
Economic and Fiscal Impact

The OTC is unable to provide information regarding the use of the program. Without information on the program’s use and the tax expenditure associate with its use, the project team is unable to evaluate the fiscal or economic impact of the program.

In order to effectively evaluate the program in the future, OTC should collect the following information:

- Amount of tax exemptions per year
- Number of tax exemptions per year
- Amount of gross proceeds from technology transfer associated with the exemption
- North American Industry Classification System (NAICS) codes associated with transferors and transferees
- Description of the technology being transferred
Incentive Benchmarking
Benchmarking

For evaluation purposes, benchmarking provides information related to how peer states use and evaluate similar incentives. At the outset, it should be understood that no states are ‘perfect peers’ – there will be multiple differences in economic, demographic and political factors that will have to be considered in any analysis; likewise, it is exceedingly rare that any two state incentive programs will be exactly the same.¹ These benchmarking realities must be taken into consideration when making comparisons – and, for the sake of brevity, the report will not continually re-make this point throughout the discussion.

The process of creating a comparison group for incentives typically begins with bordering states. This is generally the starting point, because proximity often leads states to compete for the same regional businesses or business/industry investments. Second, neighboring states often (but not always) have similar economic, demographic or political structures that lend themselves to comparison.

In the case of Oklahoma’s Technology Transfer Income Tax Exemption, only Arkansas was found to have a similar program. Arkansas’ Technology Transfer Assistance Grant Program was created in 1987 and offers grants of up to $3,750 to finance the transfer of technology from a public or private enterprise, college, university or laboratory to an Arkansas based company. Funding can be used for engineering and support fees, database searches, travel, and to pursue further grant funding from federal sources.

Arkansas’ program is similar in that it targets the costs of the transferor but differs in the chosen method of reducing costs. Instead of the tax exemption offered by Oklahoma, Arkansas offers a cash grant to fund the costs of the transfer. This is an important difference - while the overall amount of the grant is small, at $3,750 per transfer, it may be more valuable than tax preferences for the transferors of technology. Technology is most commonly transferred by non-profit research institutions and colleges or universities that are tax-exempt. In this case, the transferor may not have the tax liability to benefit from a corporate income tax exemption. Arkansas’ method of reducing the transaction costs involved in the transfer of technology may be more impactful in promoting the transfer of technology to companies within its borders.

Other Methods of Supporting Small Business Technology Transfer

More states support the transfer of technology to small businesses by offering support to small businesses and research institutions in conjunction with the federal Small Business Technology Transfer (STTR) program. This program provides funding on competitive basis to small businesses who collaborate with research institutions to develop the scientific merit of a technology and then commercialize it. Arizona and Connecticut offer training and technical assistance programs to small businesses applying for these funds. Florida provides grant funding to fund the preparation of applications for STTR funding. Both Kentucky and Nebraska offer grant funding on a competitive basis that matches STTR funds.

A key difference between Oklahoma’s program and the more commonly used programs that follow the STTR program is where the program benefit is targeted. The STTR program and the state programs that follow it are primarily focused on reducing costs for the small business that will commercialize the technology. Conversely, Oklahoma’s program provides a benefit only for the corporation that transfers the developed technology to a small business.

¹ The primary instances of exactly alike state incentive programs occur when states choose to ‘piggyback’ onto federal programs.