Economic Development: 
Equity Choices and Consequences

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ABSTRACT: In the last twenty years, economic development planning has become a major activity of state and local elected officials. So far, evaluations of planning have concentrated on efficiency—do the policies work? Given the magnitude of efforts which now reach into many foreign countries, the size of tax abatements, and value of other subsidies, it is appropriate to ask to what extent success has been achieved. Rarely have evaluations considered equity—are the policies fair? Evaluations of economic development policy must include not only “who wins,” but “who should win,” and “at what cost.” To study the policies for local government, several specific economic development projects were studied. The popular press provided the examples and illustrations of the problems and strengths. These illustrations are not rigorous case studies. Their sole purpose is to serve as examples of how a lack of clarity about the goals of policy can have unintended and unanticipated negative effects. First the case of Rio Rancho was considered. Rio Rancho is generally perceived as an overwhelming success in terms of economic development. However, a careful study of the community reveals otherwise; a city with serious financial problems due to the excessive amount of financial incentives given to relocating firms. Another example is the case of United Airlines. When United announced it would build a new repair facility, many cities engaged in a bidding war. Both the process of the bidding and the result itself provide insight into contemporary economic development planning. Finally, Disney’s America is analyzed. The issue of the bearing of risk by the firm and by government is considered. Also studied is the relationship between the local government and location decisions by the firm. The paper concludes with theorized solutions to the problems and conflicts introduced throughout the paper. A discussion of the size of tax abatements is included. Finally, the importance of the conflicts provides the conclusion.
Introduction

In the last twenty years, economic development planning has emerged as a major activity of policy makers and elected officials at the state and local levels (Bartik, 1). This focus on development was generally welcomed as it was motivated by concerns related to regional shifts in economic power and a general financial downturn during the 1980s. Systematic evaluations of economic development practice did not seem necessary in such an environment because there was a wide agreement that "something has to be done." Only recently have the first careful evaluations been conducted and published.

Thus far, evaluations have concentrated on efficiency- do the policies work? Given the magnitude of efforts which now reach into many foreign countries, the size of tax abatements, and value of other subsidies, it is appropriate to ask to what extent success has been achieved. Rarely have evaluations considered equity- are the policies fair? Secondly, evaluations have been conducted with the goals of economic development poorly defined. Two major recent texts on economic development do little more than mention some goals without ever linking particular goals to specific policy tools. Third, economic development policy examined in isolation, as if economic development goals were the only goals to be pursued by government.

The lack of explicit consideration of goals has harmed the development of sound economic development strategies, and has rendered evaluations less useful. The purpose of this project is to correct this weakness in economic development research.
Strategy

Three fundamental questions need to be asked about economic development policy: Who benefits? Who should benefit? At what cost? A recent publication Bartik (1991) addresses the first question. However, the second and third go unanswered. In light of increased competition among locations, increased value of capital subsidies, and the profound effect economic development can have on the lives of the citizens, the issue needs to be addressed.

This research contains two steps. The first part more clearly defines the goals of local and state economic development. The second part illustrates conflicts between different goals, which is often overlooked due to lack of explicitness.

A comprehensive review of literature on economic development policy was conducted to identify goals and objectives as specified by published research. The same literature was used to identify the most common tools or means of economic development and match them with the goals and objectives. Conflicts and complements were identified between different goals and objectives of government, not only in the area of economic development, but in other major policy areas. A classification of issues likely to be encountered by using current economic development tools was developed.

Based on the knowledge acquired in Step I, specific economic development projects were studied. The popular press provided the examples and illustrations of the problems and strengths identified in the first step. These illustrations are not rigorous case studies. Their sole purpose is to serve as examples of how a lack of clarity about the goals of policy can have unintended and unanticipated negative effects.
The purpose of this research was not to provide an alternate theory of economic development. Rather, it is intended to provide a conceptual framework for the evaluation of economic development policies and outcomes. In the author's opinion, such evaluations must be based on a clear understanding of the goals of economic development; only critical analysis can provide an adequate benchmark against which success may be measured. Thus, the theories of economic policy (e.g. Herbert Giersch) were widely used. The work of Tiebout on location, taxation, and government services was considered, as well as further theoretical developments based on this model. Sets of conflicts emerged as the research was conducted. One set of conflicts is between goals aimed at efficiency versus those aimed at equity. Another conflict is between the ideals of a participatory democratic process versus the needs of many specific economic development projects to be dealt with efficiently.

Defining Government Policy and Objectives

Before specific development projects or policies can be analyzed, government policy must be defined. Government policy can be characterized as multi-objective decision making; only in cases of emergency does it focus on a single goal. Giersch, in analyzing objectives, classifies them into five groups.

1. Identical Objectives
2. Mutually Exclusive Objectives
3. Competing Objectives (2 seems to be an extreme case of this class of objectives)
4. Neutral or Independent Objectives
5. Complementary Objectives (1 seems to be an extreme case of this class of objectives)
Complementary  Competing  Identical  Independent  Mutually Exclusive

At the left end of the spectrum, policies are harmonic- they are combined into a perfectly coordinated set of goals; the R (correlational) value is +1 at the far left. At the right end, goals are in complete disharmony. These goals are conflicting and contradictory; the R (correlational) value of them is -1. In the middle, goals are considered to be neither competing nor complementary; the R value is 0. Although these extremes may not exist in reality, there are certainly real examples of complements and competition. For example, there is a general belief that the government should impose some sort of pollution controls to protect the environment. At the same time, there is a general agreement that job creation should be a principal objective of government.

Conflict between these goals emerges under circumstances such as lumbering and mining. Policymakers are forced to find a medium between protecting trees and jobs created by lumbering. The same is true in the instance of protecting mineral resources and mining jobs. Federal economic development initiatives were cut for three basic reasons. First, the general attitude was that most attempts were unsuccessful. Second, there was a growing attitude that the federal budget deficit was too large and excess spending out to be eliminated. Finally, conservative ideology in public administration dominated that era, and many decisionmakers maintained that the federal government needs to remove itself from local interests. In 1988, the President's National Urban Policy Report stated: "State and local governments are increasingly sophisticated
in managing their own economics, and the federal government should in most cases avoid interfering. Although well intentioned, market intervention by the federal government has often had unforeseen negative consequences."

**Goals of Economic Development Policy**

In order to study governmental economic development policies, the fundamental goal of these policies were defined. Based on research into the purpose of the action, recurring themes emerged. Economic development policy seems to have three basic underlying objectives: (1) job creation, (2) fiscal improvement, and (3) physical improvement.

Job creation is usually considered the primary purpose of economic development policy (Elder, 1987). Many state and federal grant programs employ job creation as an explicit program goal. Employment generation is one of the most visible effects of economic development programs. As a result, it is also one of the most politically charged. When a firm shows an economic interest in an area, local officials may be committing political suicide if they fail to respond. The local governmental leaders are obligated to create an incentive package to help lure the firm or face the onslaught of criticism from the press and local constituency.

The notion of fiscal improvement is closely tied to economic development policy because the expectation is that new firms will provide more tax revenue than the additional services will cost. This fiscal advantage is the cause of much competition among localities to lure companies. In general, a region where the firm locates is the only place which derives a tax benefit from the firm's existence, unless a tax-sharing plan exists among localities. However, surrounding areas may benefit from local income tax if the workers live in that area and work the neighboring
region. Problems occur if tax incentives are offered in the form of abatements, these tax revenues are not directly generated by the firm, and the fiscal advantage to development decreases.

Finally, economic development is a way of achieving physical improvements in a community. This is a way of improving infrastructure of a locality. For example, city planners may want to attract a firm to a particular place in order to eliminate an older building, which is an eyesore. Such was the motivation of planners in the Miami area when attempting to lure United Airlines.

States are gaining more importance in the economic development arena with the continued demise of federal development initiatives. According to Fosler (1992), states have five basic economic responsibilities.

1. Establish effective legal, regulatory, and policy framework for market-driven private sector activity.

2. Provide a basic economic foundation on which the private sector depends.

3. Achieve a creative tension between cooperation and competition and resource use.


5. Tailor policies to the needs of individual regions and communities.
In a more general sense, the function of local government seems to be to provide a proper stage for economic development and then to encourage growth through the various stages of firm's development. Development is encouraged through the use of economic development tools.

**Economic Development Tools**

Many prominent instruments are used by economic development officials. Naturally, no location uses all of them. States and local governments use a mixture of the instruments, and may even change the mix depending on the particular project. According to the National Association of State Development Agency, states spent $1.5 billion in economic development enticements (Bartik, 1991). The average state has 31 incentive programs to assist businesses by providing financial assistance, tax incentives, or some sort of special service. However, the range is quite large- from only 18 in Texas to 41 in Connecticut (Hanson, 1993). Thirty five states provide job training at the request of specific companies, 49 have international involvement, and 27 have permanent offices in foreign nations (Carroll et al 1987).

One major tool used is information and marketing. Localities have started to promote themselves through pamphlets, videos, and catchy slogans like "Kentucky Means Business" or "Denver: Center of the Rocky Mountain Region" (Haider, 1992). Taking this to another level, some places have begun to make recruiting trips. Tennessee, for example, sends officials on 10-12 national recruiting trips and 8-10 international trips annually (Bartik, 1988).

Some places have created "enterprise zones." This instrument is designed to lure firms by offering them relief from regulations and certain costs of doing business. This relief is accomplished through property tax reductions, sales tax concessions, investment and employer
tax credits, and regulatory relief. During the 1980s, thirty-seven states created such zones (Isserman, 1994).

Education and technology programs have gained prominence recently. Many states have initiated programs to improve education, pointing to them as an integral part of any economic development policy (Fosler, 1988). State-supported technology programs focus on stimulating research, assisting firms to commercialize their ideas, and helping firms adopt new technologies (Isserman, 1994).

A primary subsidy tools is financial incentives. The major form is tax abatement, which is simply a waiver of taxes which would otherwise be due. Tax abatement has become the favorite tool of the government in attempts to lure firms to a region in the last 15 years. The reason being that it is believed to inexpensive, yet effective when luring new businesses (Sharp, Elkins, 1991), although other forms are available and commonly used. Tax abatement has been characterized as inefficient, inequitable, and politically controversial (Sharp, Elkins, 1991).

**Effectiveness and Conflicts of Development Instruments**

Financial incentives have been criticized as ineffective because it places regions in direct competition with each other and does not generate real economic growth (Wasylenko, 1988). Industrial policy is the "new" activity of state governments and is designed to promote business productivity through encouragement of capital formation to finance expansion (Rogers, 1994). It comes in the form of state financed research and development, incentive for capital formation in the form of grants, loans or loan guarantees, and industrial development bonds, and encouragement for international trade.
Based on concerns about this inefficiency, many regions have attempted to end interstate competition. The Committee for Economic Development generally urges states to cooperate on a regional basis. Such an agreement was in place between New York, New Jersey, and Connecticut when then Swiss Bank announced its intent to relocate. Although these three states had a covenant to compete for firms, the prospective value of the headquarters was too high to ignore. The Swiss Bank relocated to Stamford, Connecticut based on incentives.

An equity conflict arises with the overuse of tax abatement. When a community offers a firm a tax abatement, the community's tax base shrinks. If the base shrinks while the revenue requirements remain unchanged, a higher tax rate must be applied to the remaining portion. If the tax rate goes up considerably, the resulting economic climate would be discouraging to future growth. For example, what if the local government had a tax rate of $1 per unit of land and all land in use in the region was being serviced by the local government. The tax revenue was the same as the cost of the services, so the locality existed in an economic equilibrium. However, if a new firm offers to locate in the region, but asks to pay no taxes, the balance of the equation may change. Services to the firm are being provided, while the firm is not returning any money in the form of tax revenue. To correct this imbalance, the government may be forced to raise taxes to $2 per unit of land. Later, another firm may consider locating in that region, but the taxes are now twice as high as they were before. Is this fair to the second firm? What about the long-term economic health of the region? Although the regional officials and planners may have had the best intentions to help their region be competitive, the forced tax increase resulting from the first abatement has now limited the potential of the region to grow. Planners may feel limited in their choices— the firm is considering locating in their region, although the cost is too high. Too often,
the solution of the planners is to redefine the tax structure and rezone the area. The incoming firm will receive a similar tax incentive as the first firm. Again, the tax rate will change or the municipality will face a financial crisis.

**The Case of Rio Rancho and the Use of Financial Incentives**

Such is the case of the city of Rio Rancho, a "booming" Albuquerque suburb. Rio Rancho's growth is impressive, to say the least. Expanding companies, including Intel, have moved operations there. New homes are being built every day. Mayor Tom Swisstack marveled at the growth. Other cities envy the increasing wealth and economic power of the city (Tomsho, 1995).

Even so, all is not perfect in Rio Rancho. One component is clearly missing—Rio Rancho has no high school. Elementary schools and junior-high schools are packed to twice capacity. Portable classrooms have been quickly constructed on playgrounds and in parking lots. Students use outdoor toilets. Why? Because Rio Rancho cannot afford to build any new schools. Quite simply, the city has given out so many tax incentives, the municipal budget will not allow construction of educational facilities. In the words of Kent Briggs, a member of the Center for a New West (a Denver-based think tank), "when you give a tax abatement to the company coming in, either somebody else ends up paying higher taxes or the necessary public service isn't provided." In Rio Rancho's case, they chose the latter.

The example of Rio Rancho illustrates a number of points. The state and local governments do not always know what is best for them. If a city can give incentives until it cannot afford to pay for students' education, it is clearly incapable of deciding how to spent its tax
revenues. At the same time, the politicians who make those decisions are placed in a nearly impossible situation—either refuse to give the incentives and be criticized as "uncaring" (and likely lose their next political race) or offer the money to the firms and drive the city into bankruptcy. For the local governments, it is a lose-lose situation.

Further analysis of these effects can be seen through the example of the bidding war over a United Airlines maintenance facility.

**United Airlines - Competition among Localities**

When United Airlines realized that it would soon outgrow its maintenance facility in California, the firm began searching for a second location. This hunt would be called the nation's largest economic development poker game—economic planners and regional officials were all bidding for the United Airlines maintenance facility, worth an estimated $700 million. Nine cities all over the nation were attempting to lure the corporation. Fierce competition over the project existed because it was viewed as a potential source of jump-starting regional economies during recessionary times. The estimated direct push caused by the facility would be over 5,000 jobs, paying $45,000 each, to say nothing of the expected multiplier effect.

Incentive packages were offered by a variety of locations. Localities created special mixes to lure the giant facility based on that place's strengths and judgement about the firm's needs. Popular tools included tax abatement and low-cost loans.

The county that contains Oklahoma City initiated an aggressive plan to raise capital to help finance the project. Voters approved a one cent sales tax to raise $120 million over 33 months to be used to lure the firm.
Virginia promised $11.5 million per year in the form of tax, bond, and other incentives for ten years to capture the contract for facility construction from United. Due to pressure from the company, the length of the offer was doubled to $11.5 million for twenty years. Virginia estimated income from the project would exceed $27 million per year. According to Virginia State Senator Charles Waddell, "it is distasteful to get into a bidding was, but we have no choice" (Bates, 1991).

Denver began to feel like the favored choice when United Airlines announced it would move its existing operations to the new city airport and would put a reservations center and flight kitchens facility there. Other locations noted this trend with jealousy. In the words of Terry Holzheimer, the Loundon County (Virginia) economic director, "the fact that they got three out of four and got a baseball team ought to be enough."

Denver laid its hand on the table- a huge tax relief package. It would be the largest ever nationally offered for an economic development project, which included an airline-demanded $2000 tax credit for each new job it created each year for thirty years. The package also included $500 in credit for thirty years for any jobs beyond the 6,000 original jobs. Other locations noted the value of the package with awe- an estimated $360 million.

Miami, having lost a similar facility when Eastern Airlines went bankrupt, assembled an aggressive plan. The city announced it would offer a sales-tax break worth $2 million per year, an extension of an enterprise zone to allow United to receive corporate income tax credit and tax breaks on other expenses, and reduce the tax rate on aviation fuel. The package also included an already prepared site: the facility formerly housing Eastern.
Indianapolis wanted to keep its bid secret. In the final bidding, the community offer almost $300 million in incentives. Included in this package was $156.3 million in bonding the state would issue to help in construction of the base. They also had an already-prepared site for the location of the facility.

Denver, fearing tough competition, raise the stakes. Governor Romer increased the value of the plan to between $427 and $609 million. Denver agreed that it would assume $40 million in debt United owed on work at Stapleton airport. Denver also added tax breaks of its own to the plan, worth $23 million.

When the dust settled, United Airlines announced it would locate in Indianapolis, accepting the Indiana incentive package valued at $291 million.

So what does it all mean? Indianapolis surrendered $291 million dollars for a United Airlines facility because other places were willing to surrender almost as much or more. The issue now becomes is this another Rio Rancho. Did Indianapolis make the right decision?

Attraction of Business and its Costs

The fundamental issue is attraction and its costs. Rogers (1994) defines attraction as focusing industrial targeting efforts on bringing existing business from outside the region. Attraction tools were the mainstay of targeting efforts during the so-called "smokestack chasing" fad.

Mississippi is usually given credit for inventing the first state-managed program aimed at attracting manufacturing plants. Cobb (1992) describes the attraction process in great detail. From 1936 to 1940, the state successfully recruited four hosiery plants, three shirt factories, a
bedspread plant, a woolens mill, a plywood manufacturer, a tire and rubber plant, and a shipyard. The "Balance Agriculture with Industry" program offered sites and buildings in exchange for jobs and payrolls.

There are many historical precedents of successful state subsidies. During the nineteenth century, states subsidized the construction of the canal systems and railroads, thereby providing prerequisite conditions for the national transportation system. In this case, state subsidy benefitted the entire nation.

Isserman (1994) briefly mentions a very significant point. The techniques used by Mississippi are still in use today. These activities include screening prospecting companies, wooing promising firms, and subsiding new attractions. However, at that time, voter approval was mandatory before bonds would be issued to pay for the site of a building. Much more power has been given to decisionmakers to use their own judgement. Could Rio Rancho have avoided its current financial dilemma if policymakers had not had so much power? Or would the citizens have voted to pursue the aggressive financial development agenda?

Economic development bidding wars have been increasing. The value and the publicity for these projects have been growing. Data from an article by Milward and Newman (1989) can be used to track the per-job value of several automobile assembly plants.
<table>
<thead>
<tr>
<th>Date</th>
<th>Firm</th>
<th>State</th>
<th>Estimated Per-Job Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>Nissan</td>
<td>Tennessee</td>
<td>$11,000</td>
</tr>
<tr>
<td>1985</td>
<td>Toyota</td>
<td>Kentucky</td>
<td>$50,000</td>
</tr>
<tr>
<td>1986</td>
<td>Fuji-Isuzu</td>
<td>Indiana</td>
<td>$51,000</td>
</tr>
<tr>
<td>1992</td>
<td>BMW</td>
<td>South Carolina</td>
<td>$65,000</td>
</tr>
</tbody>
</table>

What if the value of the incentives exceeds the expected revenue? Such occurrences has been called "the winner's curse." That is, the cost of promoting the region and the financial incentives offer to the new plant would result in a net loss to the region (Roger, 1994).

In the United case, Colorado had some concerns that it might be offering to pay more than the project would return as externalities. Some argued that spending $360 million to create 6,000 new jobs equals spending $60,000 per new job created. According to Ed Quillen, former editor of the Denver Post, that same amount could generate 21,333 jobs in agriculture or 35,000 new service jobs. He argued that investing $360 million at 8 percent would be enough annually to provide welfare payments to 6,332 households (Quillen, 1991).

Another example of competition between localities is the case of the Swiss Bank Corporation's Move from Manhattan to Stamford, Connecticut. Citizens argued that each job moved to Connecticut would cost taxpayers of that state more than $60,000. How much is each job worth? Nobody really knows, including the decisionmakers in Connecticut.

Some would argue that decision-makers only need to take a course in capital budgeting techniques to avoid the winner's curse. However, reconsider the circumstances of the Rio Rancho case. The city planners of Rio Rancho could have easily predicted that the city would suffer a
financial shortfall in the next decade, and therefore refuse to offer any incentives to Intel or anyone else. They could have also predicted the loss of the next election and a trip through the unemployment line for themselves.

The conflict again surfaces- elected official who are responsible for making attraction decisions find themselves against the wall- either offer the incentives and jeopardize the financial welfare of the locality or lose the next election. The fear in the mind of the politician is the newspaper editorial "Mayor Refuses to Support Jobs."

The problem seems to be in the perception of the population vis à vis the goals of economic development policy. Job creation was identified as an explicit goal because it is the most visible in the eyes of the voting public. Often, the public will judge success of a project based solely on the number and quality of jobs it creates.

Returning to the Indianapolis, Mayor William H. Hudnut was elated to learn that his efforts (and tax dollars) would bring United. Twelve thousand new homes were built.

Indianapolis is considered to be one of the nation's most solvent cities, and the city has a triple-A bond rating (Abramowitz, 1991).

Where does this leave Indianapolis? Certainly, Indianapolis is large enough to absorb the cost and still provide education to students. However, the price of the facility may exceed the value of it. Only time will tell.

**Equity Conflicts in the Bidding Process**

An analysis of the United bidding process produces many relevant conflicts. These conflicts range from cost and time in the legislators to equal treatment of business firms.
Colorado was running out of time in its legislative session. With only six days left of bidding, the proposed development package required approval. In response to this, Governor Romer openly declared his willingness to call a special session of the legislature. If the assumption is that the time of legislators is without cost, then this special session is not worth noting. However, the opportunity cost of the time of the legislators is an economic cost worth studying (Gavin, 1991).

Similarly, when Virginia realized its own state laws prohibited the subsidizing of construction of the plant, the Virginia legislature went to work. Lawmakers rewrote the laws to make the state more competitive. This action is noteworthy for the same reason Colorado's legislative action is important: the time and effort of legislators is costly and limited.

Lawmakers only have a certain amount of time in their agenda. Such is the reality of the legislative process. The agenda which is pursued during that time reveals a great deal about the perceived importance of the issue. An issue which is more important will force another issue from the agenda and into the next session. How much legislative resources did Colorado use in its failed bid for United? What is the cost to the taxpayers? These are unanswerable, yet very important questions.

During the debate, Colorado legislative leader Scott McInnis stated that several companies considering locating in Colorado called him. The companies wanted a tax credit package if United received one. Providing such a package effectively reduces or eliminates that firm's debts and obligations, which can put that firm at a cost advantage. Other firms will be unable to compete at such a disadvantage over the long term. Eventually, they will seek similar deals with government so they can reduce costs and remain competitive.
Similarly, the issue of equity among firms in Colorado should be considered. Ed Quillen, a columnist for the Denver Post, asked the rhetorical question if the government wants to treat everyone equally in this nation, should the Colorado legislature be willing to give all employers $60,000 to generate a new job? Clearly, the government would not endorse such a plan (Quillen, 1991).

The reality of the United case could be reduced to such an issue- how much should local governments be willing to give firms pursuing the goal of job creation, and why are the amounts different? A primary function of government is to maintain equality. Legislative action such as the Fair Labor Standards Act or the Civil Rights Act of 1964 proves that government values equality.

The government could justify providing different subsidies to firms if data can be produced to show that a different value to the economy is provided by each job. For example, a state government might be able to furnish a larger per-job subsidy to firms which create a particular type of job over another. If electrical engineers are viewed as important to the greater economic good than janitors, the state government could justify granting a larger subsidy. However, the government should not allocate a different per-job subsidy if the jobs created are considered substantially equivalent.

Here, the difference between government and private companies is illustrated. Business concerns itself with efficiency, while government concerns itself with equity. Government often employs efficiency as a subsidiary goal. For example, because of private industry's objective of making profit, health care to the poor would never be performed. If someone who could not pay for surgery were severely injured, the hospital which performed such surgery would be at a cost
disadvantage and would soon go out of business. As a result, the government implemented a law requiring medical treatment be given to any person seriously or mortally injured regardless of ability to pay.

Another instance in which government has an advantage over private industry is defense. Having a private industry providing defense for the nation would be problematic. However, private industry has some input in the defense industry, especially in the fields of research and construction. Although these firms are private, they are closely regulated and shielded by the federal government to prevent the leakage of secret information. If such a firm were not so closely tied to the government, the profit maximization function would inevitably impact that firm, and many nation or even private individuals would attempt to purchase military hardware.

**Who Wins vs. Who Should Win?**

This paper has already defined the process of governmental decision making as being multi-objective. Firms have one basic objective: make profit, and the more, the better. Government has no such definition of success. Success of a project is measured intangibly, such as by public opinion. Defining success and failure is the goal of those studying economic development policy. To date, the general philosophy of studying the policies has been to consider the goal first, then consider who gained from the policy. Although this strategy is effective to some extent, it is far from all encompassing. In the opinion of the authors, the success and failure of governmental policy must be defined in terms of who gained versus who should have gained.

Consider the case of the Federal Housing Administration. The FHA is an agency within the Department of Housing and Urban Development (HUD). FHA was given the broad objective
to "improve the quality of housing in the nation through construction and rehabilitation." The goal of the governmental agency was to improve housing for the entire nation, but implementation was left entirely to the discretion of the agency (Meier, 1993).

FHA designed a comprehensive, yet discriminatory program. The agency set standards of acceptable housing. To enforce the standards, FHA guaranteed mortgages for houses that met their standards. Within these guidelines, millions received the loan guarantees necessary to purchase homes, making the single-family dwelling the norm for the middle-class American family.

In order to limit the losses from defaulted mortgages, certain localities in every city were "redlined." They were designated as areas where mortgages would be poor risks because of the nature of the neighborhood and other factors. Primarily, inner city and ghettos were redlined, and no federal mortgage guarantees were available to these areas. Redlining contributed to inner-city decay by denying the financial support needed to undertake rehabilitation through increased ownership.

Depending on the perspective, FHA was an unqualified success. Less than one percent of loans defaulted during that period. White, middle class Americans were able to own homes in the suburbs through the selective granting of loan guarantees.

Reconsidering the definition of success and failure, FHA could be viewed to be less than a total success. If the judgement of policy includes "who should have won," the Federal Housing Administration is less than a total success. Although many Americans received the guaranteed loans they needed to build their homes, many other Americans were denied these loans based on federal guidelines.
The "Disney Debate" and the Bearing of Risk

An example to illustrate another set of conflicts can be called "The Disney Debate." When the Walt Disney Corporation announced they planned to build a 3,000 acre theme park called "Disney's America," the residents of Prince William County in Virginia faced a problem. The new Disney park would have been a leading economic development project which would bring all the advantages of a more robust economy, as well as all the disadvantages. The county stood to gain substantial benefits in terms of population, tax revenues from one of America's largest corporations, and status. But at what cost? The residents of the county would lose quality of life, be forced to pay more in taxes to support the needed community services, and surrender part of their agricultural heritage (Berton, 1994).

After Disney announced it would not build the park, Prince William County officials asked Disney to pay $489,000 in zoning costs the county incurred. The County Executive, James H. Mullen, said that Disney's abandonment of was a violation of the "pledge of partnership" between the county and the firm. Most of the money, $340,000, was spent to organize a citizen planning task force (Washington Post, 1994).

In this case, who took the bigger risk- Disney or the county? Some of the money invested by Disney in the failed project may be salvageable- data about visitation to such a park or even public opinion and perception about such a park. The county will not likely be able to salvage any of its research- needs of such a theme park and any organizing or planning for the park.

If there was a partnership, the risk to each party would be equal. However, most firms are unwilling to engage in such a joint venture in the early stages of the development process. Why?
Because an unequal partnership exists between the two parties. Localities are forced to front more of the risk than firms.

This unequal bearing of risk can illustrated through the following model.

<table>
<thead>
<tr>
<th></th>
<th>Community</th>
<th>Firm</th>
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<tbody>
<tr>
<td>Initial Investment Outlay</td>
<td>$500,000</td>
<td>$500,000</td>
</tr>
<tr>
<td>Salvage Value if Failure</td>
<td>0</td>
<td>$100,000</td>
</tr>
<tr>
<td>Risk</td>
<td>$500,000</td>
<td>$400,000</td>
</tr>
</tbody>
</table>

In this example, the community has $500,000 at risk because there is no salvage value to the initial investment. The firm has only $400,000 at risk because there is a $100,000 salvage value.

In percentage terms, the community has 100% of its IIO at risk, while the firm has only 80%.

Why does this happen? The answer is tied to the nature of government and the nature of business. The initial investment for the locality includes research into the needs of the business and information about the particular industry in question. This information is not likely to be transferrable because it is so specific. In the Disney case, Prince William County is unlikely to ever use some of the knowledge it gained while researching Disney. In fact, the zoning costs may be losses as well, depending on the details of them. Unless Prince William County can attract another theme park, most of the expenditures are losses.

On the other hand, Disney may not have suffered a complete loss. Much of the public relations and rapport efforts with Virginia may be losses. However, some of the research may not be. For example, Disney may have studied visitation patterns to analyze how people from
surrounding communities would visit such a park. This model may be transferable should Disney consider another place.

Furthermore, business has a very organized hierarchy of decision making with all players clearly defined. In government, everyone has the right to get involved. Agenda setting frequently includes interest groups, departments, and the popular press. This all ties into the concept of democracy—the United States has a government "of the people, by the people, and for the people," which means that agenda setting and policy making are functions of the majority. One of the primary tenets forwarded by this paper is that governmental decision-making is not always the result of will of the majority. Rather, corporations have the ability to manipulate local governments based on the monetary contribution to the community through employment and tax base.

**Firms and their Location**

Clearly, large firms carry a lot of weight with the local governments where they locate or plan to locate. Companies can manipulate governments, and the relative size and importance to government of that industry dictates the responsiveness of the bureaucracy.

One example of this is the relationship between minor league baseball teams and their localities. In order for the team to remain in their current location, many are requesting or requiring that the city pay for major renovations to their existing facilities or build an entirely new facility. The city officials feel trapped between paying for these modifications and losing the team. Recently, the state of New York set aside $60 million over 4 years to help its cities avoid losing their teams. (Mahtesian, 1994).
Another instance of teams manipulating city officials is the case of Spartanburg, South Carolina. Although the city refused to build a new stadium for its team, the Phillies, the city was forced into an agreement to renovate the existing stadium at a cost of more than $1 million. In exchange, the city asked the Phillies for a long-term commitment to remain in Spartanburg from the city. The Phillies refused to sign any such agreement until Spartanburg could "increase fan and business support."

Another instance of firms manipulating local bureaucracy is Sears and Illinois. When Sears threatened to move to another state, Illinois assembled a package to "encourage" Sears to stay in the area of Chicago. The state spent $178 million ($30,000 per job) to keep the firm in a suburb (Levy, 1992).

Who Pays?

A different issue of inequity arises if it can be shown that the costs of development policies are paid by the tax revenues the less skilled and relatively less educated working class and benefit the corporation. Called an "upwardly distributive" system of allocation, this system could be an instance of the rich getting richer and the poor getting poorer. This brings on another point about the difference between government and business—government is more concerned about the equity of economics. The government actively pursues goals such as redistribution of wealth through the current (progressive) system of taxation and social welfare spending designed to benefit the lower classes of society. Business has no such programs, and having such a program would be contradictory to their goal of making profit (Steinmo, 1994).
What Can Be Done?

How can the bankruptcy of cities like Rio Ranch be avoided? A solution is to put federal regulations on the amount a locality can offer to firms. A percentage cap of their estimated tax revenues could be implemented—perhaps 10-25%. If a city had tax revenues of $1,000, it could not offer more than $250 in incentives for the next year. This might force municipalities to more closely consider how they spend their money. A federally imposed limit might be compared to an allowance. The need for this "allowance system" might be described as a weakness of the democratic/free market system. While most competition makes firms and cities stronger, this giveaway only weakens cities and slows the economy. Long-term damage is being done, and citizens are being asked to pay for it.

A growing body of evidence exists that governmental development strategies have a substantial impact on economic performance. Surveys of corporate executives show that policy enticements enter calculations when proximity to raw materials and markets, cost of energy, availability of skilled workers, and other important investment criteria are equal are in more than one location. It can be argued that if these location decision are more affected by the needs of the firm than the monetary value of the government incentive, such attempts to lure firms should make little difference (Hanson, 1993). This is clearly not the case in the instance of United Airlines, when the value of the tax subsidy was a major reason United chose Indianapolis over Denver and other locations. In fact, the reason Virginia felt it lost the valuable facility was the state government was unable to offer a large enough incentive package to United compared to
other locations (Bates, 1991). If the tenet holds that government policy does not affect business
decision locations, the next reasonable step is to pronounce development incentives to be a
wasteful use of resources. Hanson argues that this is the case.

However, it is politically impossible to not offer incentives. Those who are in the seats of
power cannot simply not offer the incentives. In the case of major projects and high profile cases,
packages must be submitted at the cost of the job of the official in the next election. The imposed
quota system might provide an adequate solution.
Bibliography


