

Literature Review of Local Economic Development Tools

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This literature review details both location-specific and tax-driven business incentives. While the more successful of these initiatives may encourage local economic development, the gains they find are not from persuading businesses to choose one dissimilar city over another, but rather to prioritize certain locations within otherwise comparable, neighboring areas. In addition, this review also notes the local environments most likely to produce these incentives.

Geographic interventions

In general, Business Improvement Districts are positively associated with economic development, while State Enterprise Zones have no association with growth. Tax Increment Financing Districts may negatively impact economic growth.

Business Improvement Districts

Once publicly approved, a Business Improvement District (BID) levies a specialized tax on all properties within the district and then independently utilizes those resources to increase public services delivered to the same area. Ellen, Schwartz, and Voicu (2007) analyzed the impact of BIDs on both commercial and residential property values. BIDs significantly increase commercial property values, although there is some distinction between the types of properties enclosed within the BID and the size of the BID. Those BIDs that are large and those most heavily populated by offices significantly increase commercial property values, while those that are small and are most heavily populated by industrial or retail properties have no significant impact. Ellen et. al (2007) postulate that, as BIDs are financed by proportional taxes levied on properties enclosed within the BID, office-dominated BIDs are able to build higher levels of revenue than retail-dominated BIDs. Interestingly, Ellen et. al (2007) also found that the creation of BIDs significantly increases residential property values, but as the BID persists, residential property values fall. The authors credit residential excitement over the potential of what the BID may accomplish for this short-term increase.

Similarly, redevelopment agencies focus development attention on a single commercial area. The *Herald-Tribune* goes so far as to suggest that very successful redevelopment agencies end up hurting the economy, as they become a well-oiled machine directing money to already-developed parts of the city (Cummings, 2015).

State Enterprise Zones

The evidence to support the economic impact of state enterprise zones is almost non-existent. Public interventions on private firms' decisions may skew their preferences to one area within a city from another, or from one type of labor market to another, but no overall increase in economic development is seen.

Ellen & Schwartz (2000) suggest that these zones attract companies from neighboring areas within a city, rather than attracting companies from one city to another. While directing employment opportunities is one goal of these zones, scholars find little to no evidence to support this. Neumark and Kolko (2010) find no evidence that such zones increase employment rates in general; moreover, the authors find no evidence that employment increases among low-salaried employees. Indeed, employees of enterprise zones do not reside in those areas, while those who do reside in such zones do not work there (Peters & Fisher, 2002). Furthermore, Ellen and Schwartz (2000) suggest that these firms could even hire outside of the state. And, if public subsidies support capital-intensive labor, these firms may decide to employ less people while investing in more automated production processes.

Tax Increment Financing Districts (TIFs)

Development in TIF districts is relatively short-lived, enduring for only a few years after creation. While one scholar has found that adopting TIF districts positively increases residential property values (Man & Rosentraub, 1998), few others confirm these findings. Dye and Merriman (2006) find that, without statistical controls, the property values of those municipalities that adopt TIF districts grows more slowly than those that do. With controls, adopting TIF districts anywhere in a city holds no impact on property values throughout the city, as “any growth in the TIF district is offset by declines elsewhere” (Dye & Merriman, 2006, p. 6). Both industrial and commercial TIF districts significantly hamper increases in values on similar properties in non-TIF areas.

It may be a case of urban predestination—the property values of those municipalities that will later adopt TIF districts grow faster prior to adoption than that of those municipalities that will not.

General Tax Relief

Similar to other incentives, reducing taxes is more likely to attract businesses to specific areas from neighboring areas than from a distant region (Ellen & Schwartz, 2000). Indeed, Bartik (1991) found that the impact of reducing taxes by 10 percent on economic development differed dramatically by region. When this reduction occurred in one state or city overall, development would increase by 3 percent in that larger area. When the reduction occurred in one specific municipality, however, that area benefitted from an increase in economic development ranging from 10 to 30 percent (cited in Weiner, 2009).

Reduced taxes also cost the public. Generally speaking, lower taxes necessitate lower levels of public service. More specifically, however, reduced taxes represent real opportunity cost for local governments. These governments must then in turn levy additional taxes or decrease spending to produce a legally mandated balanced budget (Weiner, 2009, p. 5).

Specialized Tax and Financial Relief

As taxes do not represent a significant portion of business’ costs, specialized tax relief will only attract private firms if the subsidy is especially large (Ellen & Schwartz, 2000). And, as company

strategy varies from firm to firm, it is difficult for policymakers and scholars to understand if a certain form of tax relief served as the deciding factor. Cities often offer the following tax credits to encourage business growth, to varying levels of success. Often, scholars find that the resulting local business decisions would have been made even without this weak public intervention.

State Investment Tax Credits

These credits do encourage “capital investment” (Chriniko & Wilson, 2006) but additional research suggests that companies would have made most of these decisions independently of public action (Weiner, 2009)

Research & Development Tax Credits

Wilson (2007) found that, when a state reduces firms’ research and development costs by 1 percent, that company then spends 2.5 percent more on research and development in that state (cited in Weiner, 2009). Weiner’s own research confirmed this trend, but their analysis cautions that this research demonstrates shifting investment between states, not increasing the national average.

Employment Tax Credits

A body of state-specific research posits that employment tax credits significantly, positively impacts job creation (Faulk, 2002; Gabe & Kraybill, 1999), while a few scholars find no impact (Faulk, 2002, p. 27). While Weiner (2009) highlights a body of research that suggests that these credits do impact private employment, Faulk (2002) cautions that those companies aided by this incentive would have “created a majority of the subsidized jobs anyway” (p. 27).

Industrial Development Revenue Bonds (IDRBs)

Those cities with “low property tax rates and higher technical capacity” most commonly offer IDRBs, “which cost little and attract business to cities that seem to need more business the least” (Rubin & Rubin, 1987, p. 55). Rubin and Rubin (1987) also note that offering these bonds is not connected to the cities’ unemployment rates.

Environmental Factors Encouraging Incentives

A related body of research analyzes what conditions allow local governments to pass such incentives, while another attempts to catalogue existing resources as a driver of continued economic growth.

Political viability

Rubin and Rubin (1987) highlight three categories of such incentives and the ease with which cities may pass them. Policymakers easily adopt “inexpensive” incentives, whether publicly visible or not.

These city officials may choose to hide more financially burdensome incentives through unrelated line-items. This is a very politically feasible intervention, as it is hard for the public to trace expenditures cities incur to invest in its own infrastructure in order to allow businesses to run more efficiently. In addition to attracting prospective employers, infrastructural investments create a host of additional jobs for those completing the actual infrastructural improvements. While Ellen and Schwartz (2000) suggest that the benefits of such investments are negligible, as the infrastructure of most cities is already satisfactory, they do admit that such investment may most benefit areas with significantly older infrastructure.

When incentives requiring significant public investment also require public visibility, policymakers point to the need for increased financial security and employment rates to justify these decisions to the public. Indeed, those cities home to the lowest wealth levels and greatest unemployment crises invest most heavily in expensive incentives (Rubin & Rubin, 1987).

According to Rubin and Rubin (1987), residential poverty and unemployment rates most strongly encourage businesses to incentivize business development. In decreasing importance, municipal technical capacity, a public need for city funds, and rapid growth follow as factors.

The ease with which governments may make such incentives may also be a factor. Patrick (2012) specifically studied areas' *freedom* to utilize economic incentives. In the short-run, more freedom to do so decreased growth in county-level employment. In the mid-run, such freedom decreased rural employment rates. But, within a span of five years, the freedom to utilize and pass along these economic incentives held no impact on employment or development rates.

Re-evaluating the “business-as-anchor” model

Common knowledge leads us to believe that a proliferation of small, long-running firms most strongly encourage local economic development. But the definition of small business may be under attack—the American Small Business League lists firms as large as Verizon as members; these pseudo-small businesses then receive the financial benefits that come with such a classification (Clark, 2015). And, data demonstrates that the youngest (aged 0-5) consistently produce the most jobs, and as time passes, those gains begin to fade. Firms aged 6-10 hold a neutral if slightly negative impact on jobs, while those oldest (11 or over) shift to become lose more employment opportunities than they create (Denning, 2015). A firm's youth is a much stronger predictor of job creation than size.

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