

SOME THOUGHTS ON ENTERPRISE ZONES

In the wake of this spring's disastrous violence in Los Angeles, politicians on both sides of the aisle started to scramble for some sort of policy response. The Bush administration's strategies, outlined in its 1993 budget request, re-hash some of the "market-oriented" proposals that Republican administrations have been making for the last decade. In particular, the administration proposes to revitalize our urban economies through the use of "enterprise zones."

The basic insight here - that economic incentives are stacked against investment and development in inner cities and other poverty areas - is true, and needs addressing; the question is how to do it. The president's proposal includes three specific tax incentives to stimulate business formation in the "zones". Two things seem obvious about them: that, if enacted, they will provide some improvement over the absolutely abysmal state of affairs that prevails today - and that they aren't the right way to do it.

The proposals are: 1) A 5% refundable credit on personal income tax for the first \$10,500 of wages of Zone workers earning \$20,000 or less. 2) Deferral of personal income taxes for investors who purchase stock in Zone businesses. 3) A zero capital gains rate for real estate investment in Zones held for at least two years.

Here we go again: The 5% tax credit amounts to approximately \$525 a year per individual worker. This seems all right, if we recognize that it amounts to a tax break for employers, not workers. Workers making less than \$20,000 in urban settings (where the cost of living is higher than average) are marginal workers. They are secretaries, receptionists, waiters, janitors, etc. - relatively unskilled workers of whom a ready supply exists, and who are ready to go to work for what they can get. Would the tax break make it into their take-home pay? But, the proposal would slightly lower the cost of hiring such a worker, so it might create a few more jobs.

Deferral of personal income taxes for investors in Zone businesses: the proposal makes clear that these taxes are deferred, not eliminated. They will have to be paid eventually - but! If the Zone works out as intended, they will not have to be paid until the real estate values have increased, potentially, well beyond the tax liabilities. It's easy to see that this plan could stimulate investment in the Zones. However, how will this investment benefit the people who live in the distressed communities? Since the educational level of inner-city residents tends to be low, the main force of skilled labor these developments call for will have to come from outside the community. The residents will get the marginal jobs.

Zero capital gains rate for property in Zones: this is a clarion call to land speculators. Property values in these Zones are currently very low - in fact they probably include extensive tracts of city-administered properties with negative market value. If these initiatives bring about any increase in business activity, it will be reflected in property values, and all such gains in the Zones will be untaxed. The only question here is the magnitude of the windfall. Nevertheless, this is, like the income tax defer-

ment idea, a way to bring business activity into the Zones, so that, at least, more of the residents will be able to find some kind of work.

Not a very attractive plan, so far. Is there an alternative? Well: What are some of the reasons why it is so unattractive to invest in poverty areas? There are the various social problems to contend with: crime, despair, poor health, and poor education. There is the fact that the housing stock and public infrastructure are dilapidated. And there is the financial plight of cities which, needing to provide basic social services, are compelled to penalize businesses with taxes. The Enterprise Zone plan promises a "seed" to allow progress on the first two by focusing on the third. The problem is, though, that the E.Z. plan, in the name of relieving business taxes, promises yet another public financing of private windfalls.

The evident answer to all this is to find a revenue source that does not penalize business development, which is just what we have in the land value tax! By removing taxes from improvements we remove the inherent penalty that the property tax system imposes on development. A land value tax can actually stimulate development in two ways: by making it unprofitable to hold land out of use, and by decreasing (or even eliminating) destructive wage and sales taxes.

Everyone agrees that, in the current urban crisis, some federal aid to cities is called for. So here's a new spin on Bush's "weed & seed" idea: Take a city that is in real trouble, say Detroit, or Philadelphia, or Camden, or New York (pick one). The federal government will offer this deal: if the city will quadruple its property tax rate on land only, and rescind all its other municipal taxes, the federal government will make up any budget shortfall that results. Eliminating local taxes on buildings and on consumer items will attract business and development to that city, and the federal outlay will decrease year by year until it is eliminated altogether.

There would be other benefits as well. By drastically reducing the incentive to keep land out of use, this reform will effectively increase the supply (and lower the cost) of land available for businesses to use. Many small businesses and private housing construction will become

feasible where they weren't before. By decreasing rents, and start-up costs of new businesses, there will be a greater potential for community and minority-owned businesses to get started - and therefore more people in depressed communities would have a chance to actually own a stake in the revitalized development going on there, rather than just getting a chance to wash dishes in somebody else's joint. Altogether a more healthy prospect.

Any careful reader of *Progress and Poverty* will note the Kafkaesque irony of the administration's proposal. We are going to bring cities back to life by turning selected pockets of them into enterprise zones? Is that not what cities are, in their very nature, until the cancer of land speculation starts eating at them, neighborhood by neighborhood?

-Lindy Davies

Meanwhile: The Democrats Propose "Conventionally Wise" Alternatives

The Clinton/Gore Campaign offers position papers on just about any issue the public can think of. It may be unfair to expect their recommendations to match the enforced specificity that the incumbents must present in a concrete budget proposal. But a little more definition - particularly of how they plan to pay for things - would help us to evaluate the Democrats' intentions.

Opportunity, Community, and Responsibility are Clinton's categories for rebuilding America's cities. None can argue that those aren't good things to have; but one suspects that the last two are there to soften the blow of the first, which promises to be expensive. Restoring our cities, states the Clinton/Gore campaign, demands "a new partnership committed to excellence and community service." Tax-and-spend welfare-coddlers are warned, though, that "we will make no (continued on back page)