

State's Role in Local Economic Development

A presentation for the University of Connecticut
Department of Public Policy
February 19, 2007

Office of Legislative Research
Connecticut General Assembly



Should towns offer tax breaks to attract private investment?

1. What's the state's role in helping a town decide whether to use this tool?
2. Should the state limit the tool's use?
3. Should it help towns analyze the costs and benefits of using tax breaks to attract private investment?
4. Should the state coordinate towns' (plural) efforts to attract business?
5. Should the state limit interlocal competition for private investment?

Tax breaks represent one type of economic development tool

- Tools serve different purposes or needs.
 - What purpose or need does a tax break serve?
 - What are some of the other purposes or needs economic tries to address? What are the tools associated with each of them?
- Tax breaks reduce the cost of engaging in an activity.
- They induce a business to engage in the activity now (time) and here (place).

1. What's the state's role in the use of local tax breaks

- Roles involves relationships
- Relationships are based on expectations
 - Relationships develop over time
 - Expectations become customs and traditions
 - Sometimes, customs and traditions become written rules
 - Tension develops when conditions that fostered the relationship pattern change



- Dillon's Rule: Towns are creatures of state
 - They must do the things state law requires
 - They may do the things the law allows
 - They may not do the things the law prohibits or does not explicitly authorize
- Home Rule is:
 - Tradition of local control rooted in Connecticut history
 - Tradition was reinforced by electoral system based on town-based government
 - A constitutional provision restricting the legislature's ability to pass laws affecting individual towns

Dillon's Rule Governs Local Tax Policy

- Towns can levy only those taxes state law allows—property tax and real estate conveyance tax
- Law dictates how they must assess and collect them
- It also dictates the types of property towns *must* exempt and the type they *may* exempt
- Some exemptions are permanent (e.g., churches); some are temporary (e.g., large scale development projects)
- Some are reimbursed by the state (e.g., hospitals and colleges); others are not (e.g., elderly property tax freeze)

State's role varies:

- It helps towns by allowing them to offer exemptions for different purposes (e.g., tax breaks for improving property in run-down neighborhoods)
- It collaborates with them by requiring them to grant exemptions for specific purposes and reimbursing them for the revenue loss (e.g., constructing a factory in an enterprise zone)
- It co-opts towns by requiring them to administer an exemption (e.g., manufacturing machinery and equipment exemption)

Remember: the state is a player in its own right

- Sometimes it's a free agent, lending money to businesses or allowing them to claim corporate tax credits
- Sometimes it collaborates with towns on projects by granting them money to develop industrial parks or the legal authority to acquire, clear, improve, and sell property to a private developer (i.e., redevelopment)
- Sometimes it finds itself caught between a rock and a hard place—helping a company move from town A to town B

Intergovernmental context

- State and local interests generally align (e.g., creating jobs)
- But sometimes they don't
 - A Hartford-based company tells the state it wants to relocate to a site in Farmington or Des Moines
- State and local economic development interests don't always align with other state and local goals, such as preserving farms, forests, and open spaces

Intergovernmental Context, continued

- Sometimes the state changes its programs to accommodate local goals or circumstances
- Enterprise zones
 - Initially targeted manufacturers in distressed areas in only six cities
 - Expanded:
 - More cities
 - More areas within cities
 - Other types of businesses

2. Should the state limit the use of local tax breaks?

- It does.
 - No new enterprise zones
 - MME exemption was originally a geographically targeted, limited-time exemption; then it was extended state-wide; now, a permanent exemption.
 - Development-oriented special taxing districts allowed only on case-by-case basis
- State indirectly affects the use of tax breaks by limiting towns to property taxes

Limitation or expansion: One man's ceiling is another man's floor

- The pressure to expand geographically restricted incentives tend to build over time
- Towns without enterprise zones want them. Do you think the 17 towns with the zones think the other towns should have them too?
- Battle gets fought in the legislature—need to balance general needs against specific needs
- Tension arise over a decisions made long ago about how to organize ourselves to provide public services

Ok! But should the state restrict the use of the exemptions?

- Since you asked, yes...until the we understand why more towns want them.
- Tax breaks are suppose to attract private investment.
 - Why do towns want to do this? What need does it serve?
 - How do businesses decide where to locate? How do taxes figure in those decisions?

3. Should the state help towns analyze tax breaks' costs and benefits?

- Yes, but:
 - Is there a generally accepted methodology for analyzing a tax break's costs and benefits?
 - Who should identify the costs and benefits and determine how to measure them?
 - Formulas reflect theories about economic growth
 - Why do towns need help with this?
 - Is the state in a position to help towns?

4. *Should the state coordinate local economic development?*

- Towns need to coordinate their efforts because developments in one ripple through neighboring towns
- But what should be coordinated and how?
- Why look to the state to perform this function?
 - Does the state have the capacity to coordinate local actions?
 - Are there other organizational alternatives?

Actually, the state sort of coordinates local economic development

- Here's how:
 - Large-scale, state-funded infrastructure projects affect where developers build homes, stores, and factories
 - State's public policy is to steer development away from pristine areas with no infrastructure toward developed areas where that infrastructure already exists
 - The mechanism for doing that is the State Plan of Conservation and Development
 - Recently, the plan has become controversial

The controversy is all about how to *organize* the land.

- This is the same question that defined conflict between
 - Native American tribes and the Massachusetts Puritan settlers (William Cronon, *Changes in the Land: Indians, Colonists, and the Ecology of New England* (1983))
 - Thomas Jefferson and Alexander Hamilton
 - Environmentalists and developers
 - People who live in rural areas and the people who want to live in these areas

5. Should the state limit interlocal competition for private investment...

- Are towns competing against each other?
- If yes, why? (especially when new developments create jobs and amenities for people throughout a region)
- One answer:
 - Towns use tax breaks to compete for future property tax revenue.
 - Property tax makes economic development a zero sum game for towns

and should it do so by requiring revenue sharing?

- Who's revenue would be shared?
- What are some of the potential unintended consequences of requiring towns to share some of the property tax revenue generated by new development?
- Would each town's share of the revenue be enough to reduce the competition?

Political versus Business Geography

- Competition for property tax revenue shows the difference between the political geography of mayors and selectmen and the economic geography of managers and workers.
 - Fixed municipal boundaries versus shifting market boundaries.
- Can the same be said for states?

Its time to hit the reset button...

- And think different about economic development
- Peter Senge's five disciplines can help us.
 1. Systems thinking
 2. Mental models
 3. Team learning
 4. Shared vision
 5. Personal mastery

Think Systematically

- Economic development deals with chains of events stretching back in time
- Those events involve the development and diffusion of new technologies
- The key is to understand technological change and determine its direction
- Change is a double-edged sword—it makes us anxious but it also presents new opportunities (e.g., New London)

“Check your reasoning” (R.S. McNamara)

- Systems thinking won't work unless we're willing to look critically at our mental models—our deeply held beliefs and theories about how the world works
- Economic development policies are mental models about why businesses do the things they do.
- Models often rest on unexamined assumptions (Senge's “Left-hand” column exercise surfaces hidden assumptions)

Foster learning

- Working with mental models requires us to interact differently with each other
- This requires putting advocacy in check and trying dialogue—the free flow and exchange of ideas
- Example 1992 Commerce Committee forum on enterprise zones

Shared Vision

- We need to work through our mental models to reach a common understand of what we are trying to achieve
- Right now, we could be working at cross purposes

What's in economic development for me?

- This question helps us to see how our personal baggage affects the way we look at things
- Consequently, it helps us see reality more clearly

It's more than just tax breaks

- Questions about tax breaks gets us to the core of economic development:
 - Aftershocks of rapid technological change and
 - The loss of the stable state—e.g., G. Fox in downtown Hartford; old ethnic neighborhoods
- More than new policies and organizations, we need new ways of thinking about problems and organizing ourselves for action
- And we need to constantly reexamine our theories, policies, and organizational forms in the light of new knowledge