economic development

City governments search for incentives to stimulate growth.
Economic development remains a goal of most cities, despite the slowdown caused by the Great Recession. Pictured: Boise construction workers. Next: Pueblo’s Historic Arkansas Riverwalk.
In the Urban West: Managing Growth and Decline, most of the focus was on growth, with relatively little discussion about decline. Growth was the predominant issue of the day in most cities—rapid growth, not the lack of it. Today the prospect of decline is far more a reality than it was in the 1990s. In this era of the Great Recession, many cities are struggling to provide basic services. Tempe’s budget shortfalls are the worst in the 115-year history of the city. Reno is facing such tough budget challenges that there is serious consideration to consolidate Washoe county and county governments. Modesto, in California’s Central Valley, is in a region facing the nation’s highest unemployment, hovering around 17 percent in 2010. On the other hand, the unemployment rate along the Wasatch Front, which encompasses Salt Lake City, is among the nation’s lowest, but Salt Lake City still struggles with its budget and cannot avoid layoffs and service reductions.

Cities that once seemed immune to major downturns are challenged to maintain service levels and quality of life. Boise, once the headquarters city
for several major corporations, has now lost that status. According to economic development expert Gerald Gordon, "Nothing in the economy can be taken for granted ... communities are unlikely to remain in a static economic position ... if neighboring communities are growing and yours is not, the result is not a static position, but rather a relative decline. Even modest growth may be insufficient to enable a community to maintain its quality of life."1

When prospects for growth are low, economic development competition is high. The slow or no growth voices are not nearly as effective as they are during prosperous times. Beyond the immediate economic dislocation is the prospect of a prolonged recovery and a long struggle to return to the service levels of 2007. Some veteran observers are calling this the "lost decade." The "new normal" of service reductions is no aberration. In times of economic crisis, the support for economic development initiatives are top priorities.

Since projects are often funded out of several federal sources, federal grants can play a significant role in helping a city put together an attractive offer to prospective businesses.2 "Leveraging" is an important word and practice in urban economic development. City officials have been able to use federal funds as a lever to raise additional funds from the private sector in order to help support development activities. The 2009-10 federal stimulus packages brought literally billions of dollars to state and local governments. The Build America Bond program gave cities the option of using taxable bonds and then writing down their interest rates by almost one-third with federal subsidies. Many cities took advantage of this program and improved their infrastructures. But the stimulus dollars were one-time money; federal funding to cities is becoming scarce.

On the other hand, national government policies can have a major negative effect on cities. The very availability of funds in a designated functional area can distort local priorities. Cities may expend funds for an activity or a program that would be beneficial but not necessarily essential. For example, the creation of a streetcar program may be interesting but not as important as adding more bus routes to a struggling mass transit program.

• Economic Development Goals

Growth is at the top of cities' agendas, yet it is a struggle for each city to determine what really works for its individual communities. Even though cities copy from each other all the time, what works in one city may not work in another. The factors that really contribute to economic growth may not be
available in all cities: access to markets, capital availability, skilled workforce, favorable tax policies, effective local services, high quality of life, and a business-friendly climate. Caught in the squeeze of a global economic crisis, cities may or may not be masters of their own fate.

Incredibly, economic development is championed in many communities without a clear definition of what it means. Such ambiguity may also explain its widespread popularity in some communities. According to a National League of Cities (NLC) publication, "... 'economic development' is a phrase that is widely embraced but seldom clearly defined. Conceptually, economic development has meant wealth creation to some observers, while to others, the phrase has signified material progress. As a goal, economic development ranges in meaning from tax base improvement to the redistribution of economic benefits to disadvantaged areas." It is left to each city to determine what economic development means.

Economic growth produces a sense of pride in the citizenry, a belief that the community is making progress. Often citizens want to become more involved in community affairs. To the extent that economic development is perceived as promoting jobs and expanding the tax base, it is widely supported. However, there are those communities where it is viewed as promoting uncontrolled growth with all of its negative side effects or as diverting...
community resources from other priorities and is consequently not supported as fully. The rational discussion a community should have concerning growth is typically set aside in hard economic times. But whatever the economic conditions, cities should carefully consider how growth will relate to their city’s strategic plans as well as land use plans.

Each community has to answer for itself what economic development means, what kind of economic development strategies are appropriate, and what kind of impact economic growth will have on the community. After the community has made those assessments, it can then determine the kind of economic development strategy it will employ. Will it be primarily the search for the relocation of businesses and industries from other areas, the creation of new businesses from within the community, or the expansion of existing businesses? Or will it be a combination of all of these strategies?

In addition to purely economic factors, there are other reasons for economic development competition. According to Professor Ann O’M. Bowman, our federal system, which features division and separation of powers, encourages the kind of competition we are seeing today among local communities. Federalism provides the context in which economic development is undertaken. “The interaction of federalism and capitalism structures economic development.” The American system of capitalism, with the free flow of capital across artificial jurisdiction boundaries, encourages the pursuit and competition among communities for economic development. According to Bowman,
“Cities are porous ... they are affected by the actions of other governments—national, state, and local. The economic development-related activities of these other governments structure city government’s behavior. For example, when the national government reduces Urban Development Action Grant funding or a state government creates enterprise zones, the effect is felt at

the local level. City governments have to design their economic development strategies within the ‘rules of the game’ established by other levels of government.”

- Economic Development Strategies

The economic development strategies employed by cities focus on the following in varying degrees of emphasis: attracting new businesses and industries; maintaining existing businesses and encouraging their expansion; and creating new jobs and businesses from within the community.

There are a variety of incentive packages that are offered by communities in their search for economic development. Typical incentive packages can include: technical assistance for the new business; relief from either state and/or local charges or taxes; customized job-training programs to prepare community people to work in the new businesses; public works participation through the extension of streets, water, and sewer lines to new businesses; and a “one-stop” shopping approach where new businesses can go to one office to get all of the information they need to develop or locate within a community.
More aggressive programs include tax abatements and outright gifts of land and facilities. In several Urban West states some of these incentives typically are prohibited. The granting of what can be lucrative incentives can be seen, as the proverbial phrase goes, “giving away the store.” However, providing infrastructure for a new company can make more sense than giving away land and tax relief. If the company leaves in a few years, the city is left with virtually nothing. Infrastructure, however, remains in place and is an available asset for another economic development endeavor.

Most cities employ some incentives, but the degree to which communities aggressively use incentive programs may tell a great deal about their assets in the economic development wars. According to Gordon, “... many economic development
professionals feel that incentive agreements have a place only for either exceptional prospect situations or for areas which are at such extraordinary disadvantage that no other strategy can be effective in attracting employers."9 Cities are on a slippery slope when they offer incentive packages. Once offered, precedents are set. It's hard to retreat. "This is a very treacherous practice; once begun, it becomes extremely difficult to agree to abatements or outright grants in some situations but not in others."9

Some cities have taken important cautionary measures. They have established clawback agreements, contractual agreements that provide that if companies who benefit from their incentive programs do not perform as promised, the companies will be required to pay a penalty or even, in some cities, pay back the amount of the incentive package. Enforcement is key in such arrangements. Pueblo has successfully utilized clawback provisions for a number of years. "Such performance-based incentive agreements contractually protect communities with agreed-upon reactions if forecasted job creation or investment goals are not met. This requires communities to treat
these agreements as they would any other contract.”

Elected officials walk a very thin line between offering a very liberal incentive package to an attractive company while also planning to have that company generate additional revenues to support city services. Residential properties typically do not pay for the services they consume; commercial properties pay more than their fair share, which explains a city’s commitment to economic growth.

We have numerous examples from the Urban West cities of how these individual incentives have worked. At left is a listing of economic development incentives taken from the 2009 International City/County Management Association survey of western cities. Three of the Urban West focus cities (Reno, Tacoma, Tempe) responded to the survey about which incentives they use. It is important to note that there may be state-level restrictions on the types of economic development incentives available to cities. For example, Idaho cities were not permitted to utilize tax increment financing until the state legislature authorized its use in 1988.

In trying to attract new businesses, cities attempt to develop a favorable business climate. They do not want to be viewed as being hostile to business and preclude the possibility of experiencing further growth. They want to project an attitude that is genuinely reflective of the entire community—that growth is welcome and businesses will not be frustrated by city development and regulatory policies in their efforts to grow. According to a recent NLC publication, “(f)or business leaders, time is money; they want to know that the regulatory process provides timely, reliable and transparent resolution of key issues.” The publication goes on to caution that a city should not “throw
the good out with the bad. Not all development is good development.” And that it is important to “safeguard against detrimental projects.”

City marketing strategies are often coordinated with the state economic development efforts. In this undertaking, cities can be far more specific and targeted in their efforts than can the state. As noted by Bowman, “all economic development is local.” Given the relationship of the cities to the state, state law provides the framework for whatever economic development policy a city generates. This is especially true in the kind of incentive packages a city might offer to a new business. Tax rates and types of taxes in a community are important for economic development purposes. The tax relief offered can typically only be accomplished if state law allows the city to offer such an incentive. Property tax breaks, for example, are typically set forth in state law. So are other incentives such as tax increment financing or industrial revenue bonds. These are not mechanisms that are established by cities, but by state initiative or by state constitution. State enterprise zones are another example of state initiative incentives that might work at the local level.
Economic Development Organizations

Economic development organizations take on a variety of structural and organizational arrangements. The relationship between the private and public sector varies considerably, as does the prevailing view in the community as to the legitimate role of government in marketing the community and doing economic development deals.

In some cities, the economic development function has been formalized into a municipal office or department. In other cities, the economic development organization is a nonprofit agency that may or may not have significant local governmental funding. In a 2009 ICMA study of western local governments, 74 percent of respondents indicated that the local government had primary responsibility for economic development, while 15 percent of respondents indicated that a nonprofit development corporation had primary responsibility for economic development. Four of the Urban West focus cities participated in the 2009 study. Results were available from three of those cities. Tempe reported that the local government has primary responsibility for economic development; Reno reported that they use a nonprofit organization for economic development; and Tacoma reported sharing responsibility for economic development between a nonprofit and a city, community, and economic development agency.

Economic development activities can be an integral part of the city's budget. The average amount spent by western respondents to the 2009 ICMA study was $1,813,205. The average percentage of that figure that came from local government revenue sources was 90 percent. Spending on economic development in the four Urban West focus cities that participated in the 2009 survey ranged from $75,000 in Reno to $6 million in Tacoma. Reno and Tempe reported that 100 percent of their economic development funding came from local government sources. Modesto reported that 50 percent of its economic development funding came from local government sources.
sources and Tacoma reported 70 percent from local government sources. Urban West focus cities employ a variety of local government revenue sources to fund their economic development efforts. Tempe relies solely on general fund revenues, but Tacoma utilizes nearly all the listed revenue sources (except tax increment financing and the hotel/motel tax).

While some of this variation in funding mechanism is related to local government choices and economic reality, many local governments find their choices constrained by state constitutions and legislators. Dedication of a local sales tax toward economic development often is possible only if the state authorizes the creation of a local option tax for that purpose (followed, of course, by the approval of the citizens of the local government proposing the tax). As described in Chapter 2, not all of the western states included in this study allow cities the option of creating local sales or gas or hotel/motel taxes. In those cases, the tools used for cities’ economic development are determined at the state level.

Many configurations of economic development organizations are used and some involve a mix of several types of public and private organizations: independent public agencies; private non-profit agencies; and private for-profit organizations.¹⁶ The challenge of these organizations is to develop a spirit of cooperation—a sense of unity. They need to convey to the outside world a sense of common purpose. Projecting their image underscores the importance of public-private partnerships. Government is seen as playing a key supporting role. According to a Colorado economic development corporation executive, government’s role is seen as making an area responsive to business needs. “You’re creating a product. Government isn’t necessarily the best salesman; but it has responsibility for the tax structure, the economic environment, and providing educational and training resources.”¹⁷

Of the 10 focus cities, Pueblo’s unified economic development effort stands out in marked contrast to the proliferation that is experienced in many Urban West cities. Pueblo has a public-private partnership that has worked. (See the Pueblo case study in Chapter 7 that details the city’s success and the extraordinary efforts of its economic development organization—PEDCo.)

**Effectiveness of Economic Development Efforts**

The long-term effectiveness of economic development campaigns and of economic development organizations is the subject of considerable controversy. It is hard to dispute the early effectiveness of the Pueblo Economic Development Corporation’s (PEDCo) effort in turning the city’s economy around. Losing 17,000 jobs during a 15-year period with a 1982 unemployment rate
at 19 percent, according to a PEDCo official, "(w)e had our backs against the wall." In order to accomplish a major turnaround, the community has undertaken an extraordinary effort. Former PEDCo Chairman Harold Mabie cited three major reasons for Pueblo's revitalization: (1) free land—this was offered to companies that would locate at the spacious Pueblo industrial park; (2) employee training—the president of the Pueblo community college would customize training programs for any new firm with the support of state grants; (3) "one-stop shopping"—through PEDCo the permit granting process was streamlined. PEDCo officials point with pride to the experience of two different Target warehouses—the Pueblo warehouse was in operation before the warehouse in California could get all of its permits. Some say that aggressive economic programs and incentives typically are misplaced and that their approach is fundamentally flawed. Paul Peterson notes the widespread support for economic development policies even though he asserts that much of what affects these cities, such as the welfare of the larger economy and the ultimate movements of labor and capital, are beyond their control. Scholars have noted that cities tenaciously pursue economic development, especially tax-reducing inducements to attract business, even though studies have shown that tax incentives typically are not the major factor in business location decisions. M.P. Smith, R.L. Ready, and Dennis R. Judd contend that state and local politicians are, "loathe to criticize the argument that tax incentives are beneficial, or to question the effectiveness of the other instruments that attempt to promote economic development for fear that the first to say "no" will be excluded from whatever growth does take place in the national economy." How critical are some of these incentives to the decision-making process? Are they high on the list of considerations for companies looking to
relocate? Or are they unnecessary add-ons that have no real impact, except to drain the community of resources that could be more wisely and efficiently utilized elsewhere? Judd and Kantor note that one result of economic development strategies is that, “Public poverty increasingly exists side by side with private plenty. Corporate towers, waterfront recreational development, enclosed shopping malls, luxury hotels, stadiums, and new convention centers have sprung up in cities all across America while cities struggle to balance budgets, maintain infrastructure, and provide services.”

One needs to be cautious about making generalizations about the success of these organizations and, in many cases, it may be too early to evaluate. Who knows? A judgment made about an economic development program may need the benefit of several years’ experience before its true effectiveness can be measured. According to Bowman, “Measuring success in economic development is not easy. There is confusion as to just what success is. For example, some cities point with pride at a revitalized central business district and claim successful economic development. Other cities count up the number of new firms and declare victory in the economic development wars. Others talk about renewed community spirit as a sign that economic development has been successful. One way out of this measurement quagmire is to link success to the achievement of goals.”

Looking at the Urban West focus cities, it is clear that there are some things these cities have done in the way of economic development activity that would be helpful to them whether or not they attracted any new businesses into the community. For example, the strategic planning process that many of them undertake gives them a good understanding of their strengths and weaknesses as a community.