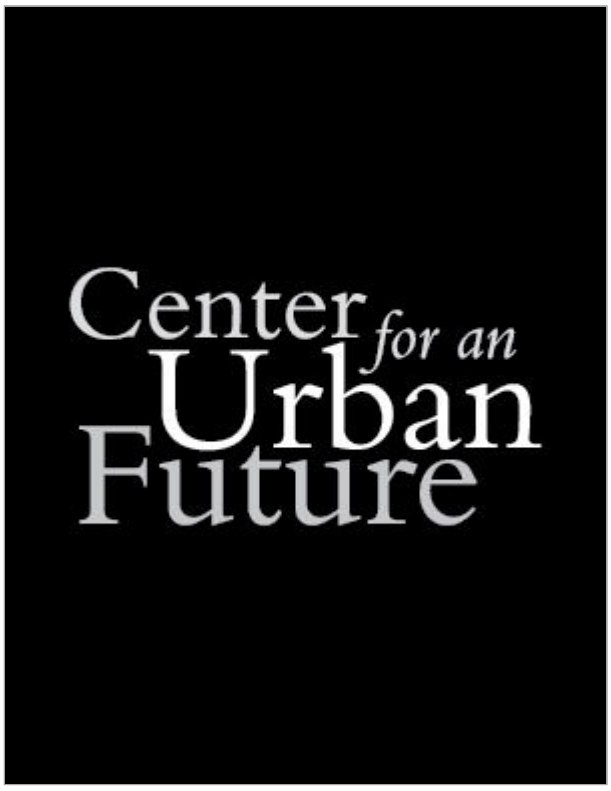


Commentary/Op-Ed - March 2002

Retention Deficit Disorder

Will New York finally adopt an incentive policy that keeps businesses in the city without giving away the store?

by Joan Fitzgerald

Call it corporate workfare.

During his campaign, mogul-turned-Mayor Mike Bloomberg made a remarkable suggestion: He proposed that companies be made to work for their government benefits.

Bloomberg recommended that the city take a good, hard look at its business-retention policies, and that it begin to develop standards to measure the effectiveness of government-subsidy deals. He also proposed that companies be made to offer something in return for incentives, and that they be held accountable if they fail to live up to their end of the bargain.

Then, on November 7, 2001, his first day as mayor-elect, Bloomberg went one better: He announced that his company, Bloomberg L.P., would reject the $14 million in tax breaks it had negotiated with the Giuliani administration.

Standards? Accountability? No more free money?

In the city's effort to retain businesses after September 11, financial incentives are a given. How refreshing that the man in City Hall doesn't think they also have to be giveaways.

Despite mounting evidence that traditional government subsidies seldom do more than pay companies for what they would have done anyway, financial incentives remain a mainstay of the economic-development strategies of many U.S. cities. Among these is New York, which has offered up more than $2 billion in corporate subsidies over the past 15 years.

These deals are regularly announced with great fanfare, but often produce less-than-model results. In 1999, for example, the

city offered StarMedia $2.5 million in tax incentives, and the state agreed to kick in $1 million, in exchange for the Internet media company's promise to boost its New York City workforce from 190 to 1,300. This produced the New York Times headline: "On-Line Network Expands," "...plans to invest $14.8 million." In 1997, the city provided a $28.5 million tax-incentive package to Merrill Lynch. New York Times headline: "Merrill Lynch to Hire 2,000 for Cash and Tax Incentives."

Not bad press for the city's economic development efforts. Never mind that the promised investments and hirings were never realized. According to "Payoffs for Layoffs," a 2001 report on corporate-retention deals released by the Center for an Urban Future, in September 2000 StarMedia announced it was cutting its workforce by 15 percent. It then released 60,000 square feet of the 100,000-square-foot office the city helped it acquire.

As for Merrill Lynch, not only did the firm not add 2,000 jobs; the company eliminated 3,400, and it moved 1,200 of 9,000 existing jobs to New Jersey within a year of signing the agreement. In January of this year, Merrill Lynch announced it would cut 9,000 more jobs globally. Although New York was not mentioned specifically, that same month the firm announced it was looking for tenants to sublet 11 floors it rents at 2 World Financial Center—450,000 square feet the company would presumably not be needing any time soon.

It gets worse. In the early 1990s, ABC made the case that the public sector should provide subsidies to firms in strategic industries even if they were not considering relocating. The city apparently agreed: It offered $26 million in tax abatements and subsidized electric power to the company in 1994. In return, ABC agreed to retain 3,700 jobs and add 185. Less than two years later, in 1996, Disney purchased ABC, immediately eliminating 60 New York management jobs in the merger, and later announcing it would cut 98 more positions. In 1999, according to "Payoffs for Layoffs," ABC relocated 240 employees from New York to California; in 2001, it laid off 15 New York network news reporters. This past year there have been cuts at Disney's ABC-affiliated Internet offices as well.

So why not just eliminate government incentives? Because sometimes subsidy deals make sense—particularly in a city with higher-than-average rents, taxes, energy costs and salaries. Without them, major companies that might otherwise stay would undoubtedly take their business elsewhere. In addition, incentives such as below-market financing or rent, energy discounts, or even tax abatements can jump-start a new sector, spur development in a struggling area of the city, or encourage a firm to expand in place rather than moving. For example, in New York, the Economic Development Corporation offers a substantial number of subsidies and tax breaks to manufacturing companies, which allow them to buy their own facilities or make needed renovations.

Economic development devolves into corporate welfare when subsidies are thrown reflexively at major corporations—however empty the threat they level—without a strategy in mind other than simply to make them stay put.

In order to make financial incentives a useful economic development tool rather than a waste of money and a burden on taxpaying businesses, the first thing the city must do is exactly what Mayor Bloomberg suggested: Make firms that receive subsidies offer something in return—and then hold firms accountable if they do not live up to their end of the bargain.

New York is not alone in its failure to hold companies to their word. In most cities, accountability—when it exists at all—means monitoring employment goals after the fact: Did a company hire as many employees as it promised? Even fewer cities or states have effective mechanisms (known as clawbacks) that respond to protect their investment when promises aren't kept.

There are, however, some localities that have drawn the line and have begun to ensure that no subsidy is just a giveaway. For example, in the 1990s, more than 67 cities or states linked development subsidies to "good" jobs, according to Greg LeRoy, director of Good Jobs First, a nonprofit that focuses on the use of subsidies in state and local economic practice. At least 16 of these cities have living-wage ordinances. Some companies have had to promise not to oppose unionization campaigns. Others have been required to provide employee benefits or give preference to neighborhood residents when

hiring.

Two other pieces of the solution are linking subsidies to the city or region's broader economic development goals, and requiring mutual investment—that is, having companies kick in some money whenever the government does.

A package put together by Chicago and the state of Illinois for Ford Motor Company, finalized in September 2000, offers a good example of the kind of deal-making New York should move toward.

The Ford plant has been in Chicago since 1933. In anticipation of a product-line switch, Ford was weighing two options: It could retrofit the existing plant—a major investment—or it could take an incentive package offered by Hapeville, Georgia, where Ford's other Taurus/Sable assembly plant is located.

Two of Ford's main concerns were improved energy efficiency and access to good transportation. The Chicago plant was old and inefficient, and located in an area with highly congested roadways—a serious disadvantage. The Hapeville package included a choice of several previously undeveloped sites near Atlanta's Hartsfield airport.

The obvious choice was to move to Atlanta, but Ford wasn't quite ready to abandon Chicago. Instead, the company requested that a developer be identified, and that the city and state work together to come up with an offer that would make Chicago competitive. Whether one sees this as Ford holding the city hostage or as the company simply making a rational decision in a capitalist economy, city and state government had little choice but to offer a subsidy package that would make the numbers work for Ford. A team consisting of the Chicago departments of Transportation, Environment and Workforce Development, and the state's departments of Transportation, Energy and Workforce Development, developed the package, with a private consultant coordinating the effort.

The $115 million package, which includes both direct expenditures and savings, does not cover the cost of the new plant itself—a measure that ensures Ford has a financial stake in the deal. Instead, it links a commitment to develop an industrial park for Ford suppliers with a plan to convert more than 900 acres of abandoned, contaminated manufacturing land in the Lake Calumet area on the city's far South Side into a center for transferring freight from one mode of transportation (rail, truck, plane, ship) to another.

The direct expenditures break down as follows: approximately $43.5 million for street and roadway improvements; $23million for workforce development; $18 million for site development; and $2.4 for energy-efficiency improvements to the Ford plant. Indirect savings to Ford come in the form of property-tax reductions, tax credits and reduced energy expenses, which will amount to $1.5 million per year.

Construction on the supplier park is scheduled to begin this spring. The new park will create approximately 1,000 new jobs and save 2,500 unionized jobs at the Ford assembly plant. The Ford plant and supplier-park firms are expected to provide $1.3 billion in tax revenue to the city and state over 10 years.

The deal has several restrictions. Ford must create a minimum of 1 million square feet of building space. The company must also guarantee that it will maintain the existing union jobs at the main plant, and that all new jobs in the supplier park will be covered by United Auto Workers union contracts. Clawback provisions require Ford to create a minimum of 500 full-time jobs by the end of 2006, and to maintain these jobs through 2011. If these provisions are not met, Ford must pay back a percentage of the financing proportionate to the percentage of promised jobs the company failed to create, and repay the city for infrastructure and road improvements.

The Ford deal includes three essential elements: linked development, mutual investment and accountability. In order to use its economic development dollars most effectively, New York should begin by establishing guidelines in each of these three areas. Then the city should go even further, and begin to establish eligibility criteria companies must meet before development deals are in the works, to help ensure that such deals are both necessary and likely to be worth the investment.

To achieve these goals, Bloomberg should appoint a permanent, independent committee charged with creating an accountability system, deciding which city economic development organizations and programs would be included, and approving all subsidies beyond an established dollar amount.

Making these changes in New York will not be easy. Part of the reason such a shaky development strategy still dominates most city and state economic-development efforts is simply politics. Politicians seeking re-election cannot afford to lose a major employer or high-profile firm on their watch. The imperative to do something, particularly if it makes headlines, drives many of these deals, which often simply delay the inevitable through the next election.

Another hurdle is that there are 25 programs offered by the city alone that offer subsidies—which include energy discounts, tax abatements and exemptions, and below-market financing or rent—in efforts to achieve different goals. These include attracting and retaining companies, facilitating expansions, promoting development in declining neighborhoods, and encouraging development of new, growth industries. This means that developing consistent criteria for subsidy deals would almost certainly entail cutting through a fair amount of red tape and resistance from the various agencies involved. But if Mayor Bloomberg takes the advice of candidate Bloomberg and follows through on this challenge, he will be taking a significant step toward getting corporations off the dole, and making them work for New York.

Joan Fitzgerald is an associate professor and associate director at the Center for Urban and Regional Policy at Northeastern University.

CENTER FOR AN URBAN FUTURE
120 Wall Street, 20th Floor, New York, NY 10005

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