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# Enterprise Zones as Tools of Urban Industrial Policy

Benedicte E.F. Mathijsen\*

Patterns of economic change in the developed world have severely hurt older urban and industrial centers. Within developed nations, large scale capital investment has shifted away from cities to suburban and less developed regions.<sup>1</sup> This exodus of jobs and economic activity from urban centers has not been accompanied by the arrival of new industries requiring similar skills.<sup>2</sup> In addition, the overall mix of economic activity in developed nations has significantly shifted toward services and away from manufacturing which was historically located in the older urban centers, leaving behind many workers with obsolete skills. Thus, many cities which grew large and powerful in the Industrial Revolution are today bastions of abandoned or obsolete facilities and high unemployment.<sup>3</sup>

Recognition of the failure of these cities to replace jobs lost to capital shifts comes at a time of difficult economic conditions and increased reluctance of central governments to support local governments economically.<sup>4</sup> Responding to the structural economic problems of their countries, governments have implemented industrial policies intended to increase national economic growth and

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1. The larger cities in the Organization for Economic Cooperation and Development (O.E.C.D.) countries are losing population while outlying regions are gaining. This is especially true for the Northeastern United States, the United Kingdom, and the Federal Republic of Germany (West Germany). ORG. FOR ECONOMIC COOPERATION AND DEV., *URBAN STATISTICS IN O.E.C.D. COUNTRIES* 42 (Feb. 1983).

2. The decline of manufacturing in cities poses an "urban dilemma": in the wake of the exodus of heavy industry, established small businesses and middle income residents have been left with the now familiar characteristics of the economic erosion of urban America, chronically high unemployment, sluggish economic growth, a declining tax base, and a smaller, less affluent group of residents who bear the rising tax rates. Cities are forced to cut back basic services which, in turn, leads to a further decline in the inner city. Solomon & Solomon, *Enterprise Zones, Tax Incentives and the Revitalization of Inner Cities: A Study of Supply Side Policy-Making*. 1981 DET. C. L. REV. 797, 797-803 (1981).

3. See generally B. BLUESTONE & B. HARRISON, *THE DEINDUSTRIALIZATION OF AMERICA* (1982); J. HUGHES, *BRITAIN IN CRISIS: DE-INDUSTRIALIZATION AND HOW TO FIGHT IT* (1981).

4. The New Federalism in the United States, for instance, has resulted in major cuts in federal programs which local governments have not been able to replace. See *infra* note 77.

productivity. The precise urban and regional consequences of these policies, however, are still unknown.<sup>5</sup>

National programs are not necessarily inconsistent with local needs and objectives, but they often fail to take into account or to correct unevenness in new investment.<sup>6</sup> In response, local governments erect programs designed to attract new industry or to slow net disinvestment, often leading to destructive competition among regions to retain or entice businesses promising jobs.<sup>7</sup>

To attract new investment to deteriorated industrial cities, thereby providing jobs and increasing the tax base, the British Government has established the "enterprise zone" program.<sup>8</sup> On the assumption that reduced business costs and regulation will attract entrepreneurs back to the inner cities, the national government designates certain regions hit by poverty to be enterprise zones where taxes are lower and regulation is reduced and streamlined.<sup>9</sup>

This note examines the operation of the enterprise zone program in the United Kingdom and considers the program's implications for the United States (U.S.), which also suffers from urban industrial decay and which has now begun studying proposals for an enterprise zone program of its own.

The note concludes that, based on the limited data available thus far, the enterprise zone program alone is inadequate to lure industry back to depressed areas. The success of the enterprise zones depends in large measure upon parallel government programs,<sup>10</sup> suggesting that the zones cannot be viewed as potential replacements of existing government aid programs. Part I of the note describes the British program and examines how it has performed in three major industrial centers. Part II discusses the leading U.S. proposal and examines its underlying assumptions. The note concludes that both the assumptions underlying the U.S.

5. See generally *Urban Revitalization and Industrial Policy: Hearings before the House Comm. on Banking, Finance and Urban Affairs*, 96th Cong., 2d Sess. 177 (1980) (statement by Walter d'Alessio, Executive Vice President, Philadelphia Industrial Development Corp., Past President, National Council for Urban Economic Development) (d'Alessio states that cities do need to be simply accommodated in an industrial policy. As centers of trade and finance, cities have a critical role to play in the design and implementation of any industrial policy, and serve as weathervanes of our economies).

6. See Glickman, *Emerging Urban Policies in a Slow-growth Economy: Conservative Initiatives and Progressive Responses in the U.S.*, 1981 INT'L J. URB. & REG. RESEARCH 492, 512-13 (1980) (Glickman warns that the burdens of reindustrialization will not be shared equally. Industrial policies often encourage further job loss in large cities and provide greater investment for already growing regions).

7. B. BLUESTONE & B. HARRISON, *CAPITAL AND COMMUNITIES: THE CAUSES AND CONSEQUENCES OF PRIVATE DISINVESTMENT* 224 (1980) (Bluestone and Harrison suggest that competition among regions, states, and municipalities for industry and jobs appears to be escalating into fierce and perhaps ruinous warfare, and offer evidence that more and more blue chip companies are taking advantage of tax incentives).

8. See *infra* note 18 for citations to the specific measures.

9. The idea was initially introduced by Professor Peter Hall in 1977 in a speech at the Royal Town Planning Institute, Chester, England on June 15, 1977. Hall intended it to be a last-ditch solution to urban problems.

10. For a discussion of the role of the enterprise zone scheme in light of ongoing public investment programs, particularly in three instances in the United Kingdom, see *infra* notes 58-73 and accompanying text.

proposal for revitalization and the proposal itself are unrealistic in their current form.

## I. THE BRITISH PLAN

The United Kingdom has fared poorly in the large structural shifts of the postwar international economy, and has experienced a significant relative performance decline in relation to other developed countries.<sup>11</sup> It has generally been unable either to compete with other advanced industrial countries in product innovation or to hold its own against rapidly developing countries in efficiency and low labor costs.

Since the industrial plant in the United Kingdom's cities typically is older and less efficient than that in outlying areas, the country's economic decline has manifested itself most dramatically in the core of its industrial cities, bringing large scale job loss and deterioration in infrastructure.<sup>12</sup> Other factors, including the failure of these cities to attract new investment and the mismatch between job skills held by urban residents and those in demand by new industry, have also contributed to the disproportionate negative impact upon cities.<sup>13</sup>

Attempting to achieve industrial and commercial regeneration through a mix of incentives and private investment,<sup>14</sup> Parliament implemented the enterprise zone plan through two statutes: the Local Government Planning and Land Act and the Finance Act of 1980.<sup>15</sup> The proponents of the plan believed that industry is responsible for economic growth and that planning rules often hamper industrial development.<sup>16</sup> They viewed the concept as an experiment in free development

11. Grant, *British Industrial Policy: Problems and its Perception*, 1982 PARL. AFF. 282, 293.

12. See generally *id.* at 282; URBAN DEPRIVATION AND THE INNER CITY (C. Jones ed. 1979); P. LAWLESS, URBAN DEPRIVATION AND GOVERNMENT INITIATIVE (1979). The rapid rate of decline in population and jobs is indicative of general distress in inner cities. Between 1966 and 1976, for example, Manchester lost 18 percent and London 16 percent of their populations. Furthermore, a greater proportion of skilled rather than unskilled people have left the cities. SECRETARY OF STATE FOR THE ENVIRONMENT, WHITE PAPER POLICY FOR THE INNER CITIES 17 (June 1977) [hereinafter cited as WHITE PAPER].

13. J. HUGHES, *supra* note 3, at 27 (Hughes describes the manufacturing crisis in the United Kingdom and the unemployment crisis that ensues when multinationals reinvest in outlying regions. He argues that adjustment of governmental intervention in the development process has been delayed and is inadequate.); N. SPENCE, BRITISH CITIES: AN ANALYSIS OF URBAN CHANGE 289 (1982) (Spence argues that although all industries have declined in inner cities, the decline is the symptom of a more general process of economic change. He further argues that the employment problem of inner cities cannot be attributed solely to environmental problems of inner cities, but to a broader reorganization of industrial production.).

14. Local Government, Planning and Land Act, 1980, ch. 65, § 179, sched. 32; Finance Act, 1980, ch. 48. The primary aim of the enterprise zone scheme is commercial and is not to bring mixtures of housing and commercial uses to the zone. The plan is not geared toward depressed residential neighborhoods; rather, the target is the old industrial areas of larger cities. Thus, the implied result is to make segregation among various land uses even more pronounced. See, e.g., S. BUTLER, THE ENTERPRISE ZONES: GREENLINING THE INNER CITIES 107-08 (1981).

15. See S. BUTLER, *supra* note 14, at 105.

16. 412 PARL. DEB., H.L. (5th Ser.) 1418 (1980) [hereinafter cited as PARL. DEB.].

similar to that which aided the rise of new economic powers such as Hong Kong and the Republic of China (Taiwan).<sup>17</sup>

### A. Rationale

The enterprise zone approach represents a shift from using traditional government grants and subsidies toward encouraging private investment as a motor for economic growth.<sup>18</sup> The government's role is to provide the proper conditions

17. Originally, the Enterprise Zone scheme was to incorporate a free trade area in which customs regulations—as in the Southeast Asian areas—were to be relaxed. The United Kingdom is limited, however, in its freedom to establish free trade areas by its membership in the European Communities. See generally S. BUTLER, *supra* note 14, at 109.

18. The Labor Party supports a more centralized planning system and opposes the enterprise zone plan. The previous Labor Administration (1974–1979) had announced a major policy initiative to deal with problems in the most blighted areas. In contrast to the Tory plan, public funds were used in a variety of different ways concentrating on job creation schemes, community groups, and recreational development. See *infra* note 57 for further discussion of the Labor Party's strategies. See Hall, *Housing, Planning, Land and Local Finance: The British Experience*, in *URBAN LAND POLICY FOR THE 1980s* 47–58 (G. Lefcoe ed. 1983). With major cuts in public expenditures, the Thatcher Government tried a different approach. The rising demands of the unemployed and the economic decline of older inner cities sparked riots during the summer of 1981 and prompted the Thatcher Government to undertake a two-tier strategy based on the enterprise zone and the Urban Development Corporation (UDC). The enterprise zone is primarily financed by the private sector, whereas UDCs are a state financed real-estate and building finance companies modeled on a type of corporation that helped build Britain's new towns. See Arnold-Baker, *Local Government, Planning and Land Act 1980: Town Development Shift*, 131 *New L.J.* 417, 418 (1981). The UDCs have the authority to deal in and develop land by acquiring both public and private land, and are able to lend money to those who intend to build on such land under the financial powers granted by the Inner Areas Act of 1978. *Id.* They also carry out building operations and allocate funds for the provision of services in the area. The UDCs are meant to encourage private participation in the revitalization of inner cities. See Purton & Douglas, *Enterprise Zones in the United Kingdom: A Successful Experiment?*, 1982 *J. PLAN. & ENVTL L.* 412, 414 (1982). They exercise the financial powers granted under the Inner Urban Areas Act of 1978 and are able to lend money to those who intend to build on such land.

The Inner Urban Areas Act also provided the legal framework within which partnerships between local and national levels of government can provide means to depressed areas for rebuilding. Most of the projects aimed at industrial regeneration came within the authority of these partnerships and contained a very wide range of employment proposals. See P. LAWLESS, *BRITAIN'S INNER CITIES* 174 (1981). The government intended to promote industrial regeneration in urban cores by getting local authorities involved. Although perhaps the most intensive administrative response to urban decay, the partnership program failed in part because of the limited amount of national government expenditure on urban programs. The partnership program was based on the premise that the effectiveness of the private sector in urban regeneration was very limited. The program's supporters estimated that the private sector would be reluctant to return to older urban areas because of a lack of commercial activity and because more attractive areas for investment existed elsewhere. Moreover, the lack of skilled labor and suitable industrial land in blighted urban areas made it unlikely that private sector investment would supplement the limited resources of urban programs. The concept of the enterprise zone, nonetheless, relies precisely on the opposite assumption, that the revitalization of inner-city areas is going to be primarily a private sector undertaking.

Criticism of the enterprise zone idea at a Conference of Social Planners suggested that increased expenditure on land, education, and social services is at least as likely to benefit inner-city residents as is unqualified fiscal support to private industries. *Id.* at 109. Furthermore, the argument went, solving the urban dilemma requires addressing the nation's economic structure, government policies, and the decisions of large companies to relocate or expand. Advances within cities would have to

under which the process of economic revival can begin.<sup>19</sup> The enterprise zone scheme arose from the perception that traditional means used by the government to create employment and stimulate economic growth, subsidies and grants to existing employers, had failed.

The Tory Government was determined to try a wholly different approach.<sup>20</sup> The Conservatives began with several articles of faith. These articles may be characterized as follows: industries are responsible for economic growth and planning measures only hamper industrial development;<sup>21</sup> the most effective way for a government to create jobs is to improve the entrepreneurial climate of a region;<sup>22</sup> because of their strong growth rates, small businesses should be the starting point for revitalization, and market forces, as judged by individual decision-makers, should determine the types of businesses to locate within the targeted regions;<sup>23</sup> finally, by encouraging companies to develop sites within the target areas, the entire local economy would benefit from the spillover of jobs and growth.<sup>24</sup> Indeed, the legislative history suggests that Parliament believed that reviving depressed areas would reinvigorate the entire national economy.<sup>25</sup>

Consistent with these assumptions, the legislation offers the private sector incentives in the form of tax breaks and reduced administrative controls. Administrative procedures were streamlined in the belief that excessive delays served only to damage the British economy.<sup>26</sup> The program was not, however, seen as a complete replacement for existing urban aid programs; aid from these programs continued to flow into the zones.<sup>27</sup> Indeed, the legislation establishing enterprise zones was not part of the Tory Government's regional or inner city programs.<sup>28</sup>

"concentrate on greater public control of industrial production, subsidized housing markets for poorer inner area residents, and on integrating more disadvantaged groups into the process of decision-making." *Id.* at 195.

19. The critical problem is that much of the innovative entrepreneurship, once the most important economic feature of central metropolitan areas, has disappeared as cities have decayed. See S. BUTLER, *supra* note 14, at 96. See also *infra* notes 23, 30, and 47.

20. Purton & Douglas, *supra* note 18, at 413.

21. J. STAMBOLLOUIAN & I. McDONALD, U.K. ENTERPRISE ZONES 14 (Lincoln Institute of Land Policy, Land Policy Roundtable Basic Concept Series No. 103, July 1982).

22. See Arnold-Baker, *supra* note 18, at 417-18 (the purpose is to secure regeneration by developing land and creating attractive environments so as to attract more industry and commerce). See, e.g., *Back to the 19th Century*, NEW STATESMAN, July 11, 1980, at 42 (inner cities are turned into areas free of certain taxes, rates, and planning controls in order to enable entrepreneurs to start up businesses and help revitalize British industries).

23. See Purton & Douglas, *supra* note 18, at 417 (statement by Secretary of State from Wales); see also J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 3.

24. See Davies, *The Inner City in Britain*, in *ADVANCED INDUSTRIALIZATION AND THE INNER CITIES 7* (G. Schwartz ed. 1981); *URBAN ENTERPRISE ZONES: INNER CITY PANACEA OR SUPPLY-SIDE SHOWPIECE?* 16 (Lincoln Institute of Land Policy, Land Policy Roundtable Basic Concept Series No. 105, 1982) (stating that the Tory government's reliance on supply-side policies is based on the assumption that tax incentives alone will create a dramatic turnaround) [hereinafter cited as *SUPPLY-SIDE SHOWPIECE*].

25. PARL. DEB., *supra* note 16, at 1518.

26. See S. BUTLER, *supra* note 14, at 140.

27. Existing programs are discussed in greater detail in the British case studies *infra*.

28. J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 14.

## B. Operation

Advantageous rules for tax and planning purposes are the main benefits to locating in an enterprise zone. Under the Finance Act of 1980, a number of activities conducted within the zone are exempt or enjoy reduced taxation.<sup>29</sup> Other benefits of the zone include planning and tax concessions under the Local Government, Planning and Land Act of 1980.<sup>30</sup> Industrial and commercial properties are exempt from local authority taxes, except for taxes on water, with the national government reimbursing the local authority for any loss.<sup>31</sup> Firms may take a 100 percent deduction against income for tax purposes for capital expenditures on plant and machinery and 50 percent deduction for construction, extension, or improvement of industrial and commercial buildings. Offices, shops, and other commercial buildings receive no benefits.<sup>32</sup>

Firms in enterprise zones receive priority for special customs facilities. They need not submit information to Industrial Training Boards and are exempt from their levies.<sup>33</sup> The planning process for zones is simplified, with the government demanding less statistical information. For each zone, a plan is prepared setting out the types of developments for which permission is automatically granted.<sup>34</sup> For developments that do not conform and thus, require individual variances, applications will be expedited.

The power to select regions as enterprise zones rests in London's administrative discretion, upon consultation with local authorities. The government considers the severity of the economic problems in the area, the failure of past special measures to ameliorate the difficulties, the interest shown by local authorities, and the availability of land for development.<sup>35</sup> The local authorities must prepare a planning scheme and comply with statutory requirements for consultation with adequate public notice.<sup>36</sup> Local authorities must also be prepared to defend the planning scheme in the courts and in Parliament. Since 1981, the Secretary of State, who manages the enterprise zone program, has designated eleven areas to be established as enterprise zones for ten-year periods.<sup>37</sup> Sites, which had to show development potential, were selected in different regions in the United Kingdom to test the effectiveness of the enterprise zone approach in differing circumstances.<sup>38</sup>

29. Finance Act, 1980, ch. 48. For example, real estate developers operating in a zone are not subject to the 60 percent tax levied upon the development value realized from selling an interest in land. *Id.* at 110.(1).

30. Local Government, Planning and Land Act, 1980, sched. 32, 27.(1) and 29.(1).

31. *Id.*

32. *Id.*

33. REFERENCE SERVICES, CENTRAL OFFICE OF INFORMATION, PUB. NO. 140/82, BRITAIN'S ENTERPRISE ZONES AND URBAN DEVELOPMENT CORPORATIONS 2 (June 1982).

34. *Id.*

35. The sites are approximately 500 acres each. S. BUTLER, *supra* note 14, at 110.

36. *Id.* See also Local Government, Planning and Land Act, 1980, ch. 65, § 179, sched. 32, 2.(2), 2.(3), 2.(6).

37. Enterprise zones have been established in Corby, Dudley, Hartlepool, Isle of Dogs, Newcastle, Trafford, Speke, and Wakefield in England; Lower Swansea Valley in Wales; Clydebank in Scotland; and Belfast in Northern Ireland. REFERENCE SERVICES, *supra* note 33, at 1.

38. In determining the development potential of an area, the national government expected local

### C. Criticism.

Analysts, business leaders, and the opposition have expressed a number of doubts about the enterprise zone program.<sup>39</sup> First, the evidence indicates that it is extremely difficult in the United Kingdom or in the United States to entice industries to locate in central cities due to the uncertainty of demand there, the growth in outlying regions, and the rapid decline of urban infrastructure.<sup>40</sup> The opponents of the bill feared that communities would fight for an enterprise zone designation. By competing with one another to win more companies and jobs, they would relinquish control over important regional functions.<sup>41</sup> Not requiring a planning application from incoming businesses would be dangerous. Some activities might affect important rights of the local population without the protection of governmental review or the possibility of a planning appeal.<sup>42</sup>

During parliamentary debates, some members of Parliament also feared that the enterprise zone would benefit those organizations and businesses that do not need assistance.<sup>43</sup> The legislation would enable private entrepreneurs to produce makeshift schemes to "provide a few miserable jobs in areas where the standards would be less than adequate."<sup>44</sup>

Some industrialists were concerned that the boundaries of the enterprise zone would create unfair competition by arbitrarily providing incentives to some and not to others.<sup>45</sup> Thus, some firms would benefit from rate concessions by fortuity of location without having made any prior investment commitment to the zones.

The lack of government control over the type of enterprise attracted to the zone poses several dangers.<sup>46</sup> Some private decisions stimulated by the program may have deleterious effects within the zone or adjacent areas. For example, if growth of a zone is the result of firms relocating rather than starting up, the "vacuum effect" on outlying regions may simply lead to the restructuring of investment rather than to an increase in output overall.<sup>47</sup> The government concedes that

governments to show their willingness to enact similar provisions to reduce taxes and streamline regulations. SUPPLY-SIDE SHOWPIECE, *supra* note 24, at 2. J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 4.

39. PARL. DEB., *supra* note 16, at 1478.

40. *Id.* at 1459.

41. *Id.* at 1505-7.

42. *Id.* at 1467.

43. *Id.* at 1451.

44. *Id.* at 1448.

45. Butler questions the inclusion in the package of firms that do not generate jobs and do not expand. S. BUTLER, *supra* note 14, at 118; J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 6, 7.

46. See generally SUPPLY-SIDE SHOWPIECE, *supra* note 24, at 10 (stating that greenlining sites may make zones thrive merely at the expense of neighboring areas whose jobs and resources are lost to the designated site). According to a critic, zones "are likely to have little impact on the level of economic activity, appear to be based on a fundamental misconception of how labor markets operate, and are likely to influence the distribution of commercial activity in a manner which will impose substantial disadvantages on existing traders." *Enterprise Zones 'Unlikely to Help Economy'*, The Times (London), July 31, 1980, at 18.

47. The Minister for Local Government Affairs stated that any of these assistance and promotion schemes run the risk of attracting firms from elsewhere; however, the issue is whether the scheme can stimulate growth of new enterprises. P. LAWLESS, *supra* note 18, at 181.



relocation is bound to occur under any program that provides benefits to a small area.<sup>48</sup>

The enterprise zone plan focuses on larger corporations as potential agents for investment in the targeted areas. The plan's incentives are geared exclusively to large corporations and operate to the advantage of property owners and developers but not local residents.<sup>49</sup> Yet, small firms may be more successful instruments for urban regeneration.<sup>50</sup> The plan fails to address the needs of small businesses, which are usually in low marginal tax rates and which lack start-up funds to acquire equipment and make other capital expenditures.<sup>51</sup> Small businesses rarely undertake construction projects and lack profits against which tax allowances can be taken.<sup>52</sup> Even so, one of the plan's principal components is reduction of taxes. The scheme also fails to include measures for training unskilled workers. This is a critical omission in view of the need most small businesses have for skilled labor.<sup>53</sup>

In summary, the tax-cutting focus of the plan appears inadequate to create jobs in depressed areas. Moreover, the assumption that the jobs and the firms appearing in target areas will be a net gain to the national economy is open to dispute.<sup>54</sup>

Labor unions have strongly objected to the enterprise zone legislation because they perceive it to be a direct threat to the entire labor movement. Indeed, the initial proposals even included waivers, later dropped, of minimum wage rules. The suspicion that these early proposals would resurface led the unions to fear that lack of enforcement of existing safety laws would lead the firms to violate workers' safety laws.<sup>55</sup> Because of the danger of deterioration in worker safety,

48. See, e.g., Aronowitz & Goodman, *Ghetto Enterprise Zones: A Walk on the Supply Side*, NATION, Feb. 21, 1981, at 207 (stating that the enterprise zone legislation reflects the government's effort to apply supply-side economics to social problems and an update of an early industrial proposition that what is good for business is good for the country). Basically, the proponents reason that rapid growth in the 19th century was associated with an absence of government regulations and a very low level of taxation, and that by reintroducing similar conditions, investment can be attracted in decaying inner cities. See generally *infra* note 80, at 5 (statement by Marc Bendick, Jr., economist with the Urban Institute).

49. S. BUTLER, *supra* note 14, at 121, 142; P. LAWLESS, *supra* note 18, at 181.

50. See Birch, *Who Creates Jobs?*, 1981 PUB. INTEREST 3 (Birch argues that all new job opportunities in the United States are products of small businesses and that rapid economic growth has been characterized by a high rate of new small firms. Since growth did not occur in larger corporations, small firms appeared to generate growth.). *Contra* B. BLUESTONE & B. HARRISON, *supra* note 3, at 221 (arguing that the tendency towards deindustrialization among large corporations—principally through foreign investment, mergers and diversification—means that by default the growth that did occur took place in smaller businesses).

51. See *infra* notes 113–114 and accompanying text for further discussion on small business.

52. See S. BUTLER, *supra* note 14, at 120–22.

53. Solomon & Solomon, *supra* note 2, at 818.

54. P. LAWLESS, *supra* note 18, at 174.

55. "The firms would try to weaken rights of workers, especially in relation to unfair dismissal and union recognition." *quoted in*, S. BUTLER, *supra* note 14, at 113 NATIONAL EXECUTIVE COMMITTEE ON THE LABOUR PARTY, ENTERPRISE ZONES 6 (1980). Although the proponents of the bill agreed to delete any suggestion in the bill that minimum wages be reduced, labor unions feared that enterprise zone deregulation would still weaken worker rights, safety, and union deregulation. Under the legislation as passed, enterprise zones benefit from simplified planning and building controls but they are not free from controls on environmental pollution, health, and safety. Hall, *supra* note 18, at 54.

the press characterized the concept as a return to 19th century conditions.<sup>56</sup> The trade union opponents seek primarily the creation of more jobs and the raising of the average skill level of workers.<sup>57</sup>

#### D. Examples

To illustrate the operation of enterprise zones, this note will examine three cases. Evaluation of the results of each zone is incomplete, and available information is sparse. The results available thus far indicate achievements only in site preparation and rehabilitation of existing structures.<sup>58</sup>

##### 1. Manchester

A heavily industrialized city, Manchester has lost a large number of manufacturing jobs in the last decade, and is consequently experiencing a drop in its population.<sup>59</sup> Plants have shrunk or closed as relative productivity has fallen, facilities have become outdated, and structural declines have hit certain types of heavy industry concentrated in Manchester.

Three enterprise zones were designated in the Trafford Park Industrial Estate (TPIE), an industrial development region in Manchester, and will operate there for ten years.<sup>60</sup> Simplified planning and regulatory criteria ensure speedy handling of applications for location in the zone. The greatest benefit of the program

56. PARL. DEB., *supra* note 16, at 1478.

57. The previous Labor Administration announced in 1977 a major policy initiative to deal with the problem of inner city decay and unemployment. WHITE PAPER, *supra* note 12. By granting explicit priority in social and economic policy to inner areas, the Labor Government tried to tailor programs to the specific problems of individual cities. The premise of the White Paper is that measures can be taken in order to avoid displacement of existing industries and encourage stabilization and development of all firms.

The Labor party identified employment as the main problem of cities. Low demand for labor was particularly severe in inner cities, which traditionally have a significant concentration of unskilled and semi-skilled workers. As important as employment is, however, it seems apparent that the real test of success of an urban scheme is the degree to which residents' life has improved overall. This would seem to dictate some emphasis on housing where physical decay is especially relevant. However, the enterprise zone ignores housing.

The White Paper sets forth four basic aims to reverse decay and unemployment: economic, physical and social improvement and a balance of population and jobs between inner areas and outlying areas. The means chosen to implement these goals is increased public investment with more emphasis on jobs, training, the environment, and improvement of existing housing. Under this approach, the private sector would be encouraged to invest in and direct government investment would be applied to areas with major structural problems.

58. Most of the information available through the local administration of the zones is promotional and does not include overall growth in employment or firms.

59. See, e.g., Dicken & Lloyd, *The Corporate Dimension of Employment Change in the Inner City*, in URBAN DEPRIVATION AND THE INNER CITY 34 (C. Jones ed. 1979). This trend is not limited to Manchester. Preliminary returns from the 1981 Census indicated that 1.5 million persons left major British cities for outlying regions.

60. Before the enterprise zone program began, the TPIE enjoyed "intermediate area status" under an earlier aid program embodied in the Inner Area Act. The tightening of criteria cost the region this status and deprived it of government grants toward the cost of building manufacturing sites. P. LAWLESS, *supra* note 18, at 140.

to local businesses is that local authority property taxes are suspended until 1991.<sup>61</sup>

A recent Trafford Policy Committee report, outlining the principal problems of the zone, concluded that the zone had succeeded in creating and retaining employment opportunities.<sup>62</sup>

[H]ad it not been for the Enterprise Zone status of certain areas of the [TPIE], a fair proportion of new companies would have moved elsewhere, and, in some instances, certain companies would have only contemplated closing. The local officials feel that the designation of an Enterprise Zone draws the attention of industry to the benefits of investing in the Borough.<sup>63</sup>

## 2. Clydebank

Clydebank, a major industrial city in Scotland, fell upon hard times with the 1979 closure of the giant Singer works as markets for sewing machines and ocean liners declined and lower-cost producers entered the market.<sup>64</sup> The Scottish Development Agency (SDA) poured money into the area prior to its designation as an enterprise zone, offering incentives to encourage redevelopment.<sup>65</sup>

Seen as complementing, but not replacing the activities of the SDA, the zone program publicizes the various benefits available to companies locating there and provides worker training to teach skills required for changing technology.<sup>66</sup> The SDA also established an enterprise zone fund offering commercial loans to companies with the potential of creating new jobs.<sup>67</sup> Clydebank also benefits from the nation's highest rate of regional and inner city assistance.<sup>68</sup>

While it is difficult to separate the results of the zone from those generated by the SDA, the combined package has shown impressive results. Over 2,000 new jobs were projected for the end of 1983, half of which were generated by newly established firms.<sup>69</sup> This growth stimulated considerable demand for small facili-

61. See J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 12. Exemption from industrial and commercial property rates promote private investment and development of land. This approach is a significant departure from earlier programs where the government would claim and rehabilitate the land to stimulate private investment.

62. POLICY COMMITTEE, TRAFFORD BOROUGH COUNCIL, INDUSTRIAL DEVELOPMENT—ENTERPRISE ZONES—EFFECTS OF LOCAL MONITORING PROCEDURES, REPORT OF THE CHIEF EXECUTIVE 3 (Apr. 19, 1982).

63. *Id.* at 3; Trafford Park Enterprise Zone Scheme, Metropolitan Borough of Trafford (May 28, 1981); Letter to author from R.M. Dodsworth, Industrial Development Officer, Trafford Enterprise Zone (Nov. 4, 1983) (copy on file, Michigan Yearbook of International Legal Studies).

64. Dicken & Lloyd, *supra* note 59, at 59 (reporting on a study that in a recession, plant closure has been the more frequently chosen option than the alternative of shedding labor and maintaining plants that run below effective capacity).

65. The Clydebank Task Force was set up in order to stimulate investment in the zone. Letter to author from J. Cunningham, Development Officer, Clydebank Task Force (Nov. 2, 1983) (copy on file, Michigan Yearbook of International Legal Studies). The growth identified by the Task Force is in industrial promotion investment, factory building, environmental improvement and small business advice. CLYDEBANK TASK FORCE, POSITION STATEMENT 2 (Sept. 1, 1983).

66. J. STAMBOLLOUIAN & I. McDONALD, *supra* note 21, at 7.

67. CLYDEBANK TASK FORCE, *supra* note 65, at 4.

68. S. BUTLER, *supra* note 14, at 114.

69. CLYDEBANK TASK FORCE, *supra* note 65, at 2.

ties. This is in contrast to the city's surplus of giant plants. To redress this imbalance, the SDA invested significant amounts of money to develop small units.<sup>70</sup> The Clydebank experience demonstrates the interdependent character of several urban aid programs.

### 3. London

The Isle of Dogs, located in London's former dockland area consists of former docklands, dock basing warehouses, and vacant land.<sup>71</sup> The closing of docks and transfer of port activities elsewhere led to economic decay and the designation of the area as an enterprise zone in May 1982.

Much of the land in the area is owned by the London Docklands Development Corporation (LDDC), which is implementing a multifaceted development program for industrial, recreational, and residential development.<sup>72</sup> The LDDC itself converts sites and markets them according to the goals of maximizing job creation and of conforming new construction to the LDDC's master plan.<sup>73</sup> The LDDC also has cut planning requirements to speed project completion and is currently in the process of expanding its services generally. Since designation as an enterprise zone is only a small part of a larger program, assessment of the zone's results is difficult.

## II. THE AMERICAN PROPOSAL

Responding to a trend of inner-city industrial disinvestment in the United States,<sup>74</sup> the Reagan Administration introduced the Enterprise Zone Employment

70. CLYDEBANK TASK FORCE, HISTORICAL SUMMARY AND SITUATION REPORT 4 (Nov. 1980).

71. The regeneration of the London Docklands is under the control of the London Dockland Development Corporation (LDDC) set up in 1981 to improve employment, housing, shopping, and recreational facilities to benefit the area and, ultimately, London. The enterprise zone is, therefore, part of a larger project that also includes special incentives for industries and companies that are outside the zone. So far, a third of the 750 newly created positions are within the zone. *See ISLE OF DOGS ENTERPRISE ZONE, THE GUIDE* 12 n.d.

72. P. LAWLESS, *supra* note 18, at 260.

73. Special engineering studies carried out for building purposes are made available to prospective developers.

74. *See generally* Hicks, *National Urban Land Policy: Facing the Inevitability of City and Regional Evolution*, 5 *URB. L. & POL'Y* 235-53 (1982) (discussing the transformation of urban industrial America); *see also* Schwartz, *Urban Policy and the Inner Cities in the United States*, in *ADVANCED INDUSTRIALISATION AND THE INNER CITIES* 47 (G. Schwartz ed. 1981) (asserting that central cities are no longer the primary competitors for growing industries and businesses); N.Y. Times, June 9, 1980, § 1, at 18 (quoting Professor Kasarda at a symposium of the President's Commission for a National Agenda for the 1980s, saying that although massive centralized industrialization is over, cities continue to play important roles as financial management and entertainment centers despite deterioration in residential areas and personal income levels; N.Y. Times, Jan. 3, 1983, § 1, at 15 (cities have been hit harder than in any downward economic turn since World War II). The 1980 census figures show widening disparities between residents of central cities in metropolitan areas and residents of surrounding suburbs, not only in income but also in employment, housing, living arrangements, and family structure. Cities and suburbs combined represent three-quarters of the nation's population. The current recession, however, has worsened the disparities in income with central city residents bearing the brunt of layoffs and reductions of federal aid. A Brookings Institute Study suggests that downtown renewal and gentrification are not sufficient to reverse the decay in older cities. N.Y. Times, Feb. 27, 1983, § 1, at 1, col. 2.

and Development Act of 1983,<sup>75</sup> a package of tax cuts and regulatory relief to amend the Internal Revenue Code.<sup>76</sup>

### A. Rationale

The goal of the proposed legislation is to revitalize economically decaying urban areas without involving the federal government in the development process.<sup>77</sup> The federal government establishes the environment for local development strategies by providing incentives rather than subsidies.<sup>78</sup> The government bases the assumption of viability of state-established enterprise zones on the premise that enterprise zones at the local level will effectively complement federal incentives.<sup>79</sup>

The enterprise zone scheme would not replace existing aid programs, such as development grants, loan guarantees, and job training programs. Instead, enterprise zones seek to stimulate small businesses not covered by existing pro-

75. The Administration's bill was introduced as S. 98 and H.R. 1955 in Congress. S. 98, 98th Cong., 1st Sess. (1983); H.R. 1955, 98th Cong., 1st Sess. (1983) [hereinafter cited as H.R. 1955]. Two other bills on the enterprise zone proposal will not be discussed here: The Community Assistance and Revitalization Act of 1983, S. 863, 98th Cong., 1st Sess.; H.R. 1735, 98th Cong., 1st Sess.; and the Enterprise Development and Industrial Revitalization Act of 1983, S. 634, 98th Cong., 1st Sess.

The 1982 proposals introduced in the 97th Congress are discussed in Note, *Federal Enterprise Zone Proposals: Incentives to Revive Our Decaying Inner-cities*, 10 J. LEGIS. NOTRE DAME 425 (1983).

During the 98th Congress two hearings were held on the enterprise zone legislation before the Senate Finance Committee and the House Ways and Means Committee. See *infra* note 80. No action was taken on any of the bills by the end of the session, October 12, 1984. In his State of the Union address, President Reagan urged Congress to pass the enterprise zone legislation. STATE OF THE UNION—ADDRESS BY THE PRESIDENT OF THE UNITED STATES, H.R. DOC. NO. 25, 99th Cong., 1st Sess. 322, 323 (1985). So far, one bill has been reintroduced in the House by Congressman McDade. Enterprise Zone Employment and Development Act of 1985, H.R. 38, 99th Cong., 1st Sess.

76. The specific form of the legislation is a series of amendments to Title 26 of the U.S. Code, the Internal Revenue Code. Among other changes, the bill would add a Subchapter C, Designation of Enterprise Zones to chapter 80, and would add a section 44H, Credit of Enterprise Zone Employment, to Subchapter A of chapter I. Currently, the Code contains only a few provisions giving special tax treatment to specific geographic areas. For example, rules for mortgage subsidy bonds are more liberal in certain areas for the purpose of promoting housing development. I.R.C. § 103A (1983).

77. This involves a policy decision setting forth the appropriate roles of government in providing assistance to metropolitan areas. The approach of the Reagan Administration was summarized in an Urban Policy Paper urging cities to save themselves. N.Y. Times, July 14, 1982, § 1, at 1. The press quickly accused the federal government of abdicating responsibility. See, e.g., *id.* at 17. Eventually, the President repudiated the policy paper.

A recent survey indicated that despite enduring layoffs of city employees and higher taxes, cities are not able to replace cuts in federal aid with local funds. N.Y. Times, Jan. 3, 1980, § 1, at 15, col. 1. Furthermore, the oldest cities are continuing to decline and economic activities have been too small to boost the aggregate level of prosperity. N.Y. Times, July 7, 1980, § 1, at 1. It has been argued that the single most important contributing factor the cities' growth is the federal government's encouragement of their economic development. Huth, *New Hope for the Revival of America's Cental Cities*, ANNALS, Sept. 1980, at 118.

78. S. BUTLER, ENTERPRISE ZONES: TIME TO ACT (Heritage Foundation Issue Bull. No. 100, Nov. 17, 1983).

79. See *infra* note 87 for state enterprise zone schemes.

grams,<sup>80</sup> by reducing the real cost of wages and investment and by streamlining regulation. The tools to be employed are tax incentives for hiring workers and for making investments in enterprise zones, and procedures to waive or modify certain federal agency rules to facilitate economic development.<sup>81</sup> The bill's rationale is that economic activity will respond favorably to tax breaks and reduction in regulation.<sup>82</sup>

### B. Operation

The Department of Housing and Urban Development (HUD) would administer the program.<sup>83</sup> After local and state governments nominated the zones, the Secretary of HUD would designate the zones for a ten-year period with possible extensions.<sup>84</sup> The Secretary would ensure that the area meets the requirements of an enterprise zone. Selection would depend upon the degree of local commitment to redevelopment and certain levels of poverty, unemployment, economic and general distress, or noticeable decline in housing and population over the preceding ten years.<sup>85</sup> The local government would have to demonstrate its commitment to revitalizing the area by tailoring its own regulatory program and implementing the objectives of the scheme.<sup>86</sup>

In seeking further support for the federal proposal, HUD cites several state-implemented zones. In particular, the Administration cites the progress achieved by the states in laying down the foundation of the enterprise zone legislation.<sup>87</sup>

80. *Enterprise Zones—1983: Hearing before the Senate Comm. on Finance, on S. 98, S. 634, and S. 863, 98th Cong., 1st Sess. (1983)* [hereinafter cited as *Senate Hearings*]; *Enterprise Zones: Hearings on H.R. 1955 before the House Committee on Ways and Means, 98th Cong., 1st Sess. 2 (unpublished, Nov. 17, 1983)* (statement by Congressman Jack Kemp) [hereinafter cited as *House Hearings*.]

81. H.R. 1955, *supra* note 75, at § 101(a) (I.R.C. § 7871(d)(2)). Throughout this note, references to provisions of the Reagan proposal will be made first to the sections of the bill and then, parenthetically, to the Internal Revenue Code that they would amend.

82. *Senate Hearings, supra* note 80, at 215 (statement by Senator Rudy Boschwitz).

83. H.R. 1955, *supra* note 75, at § 101(a) (I.R.C. § 7871 (a)).

84. *Id.* § 101(a) (I.R.C. § 7871 (b)).

85. *Id.* § 101(a) (I.R.C. § 7871 (c)). The area must be within the jurisdiction of the government nominating it, of a certain size (population of at least 1,000), and of a certain poverty level, JOINT COMM. ON TAXATION, 98TH CONG., 1ST SESS., DESCRIPTION OF BILLS (H.R. 1955, H.R. 1735, AND H.R. 2375) RELATING TO DISTRESSED AREA TAX INCENTIVES SCHEDULED FOR A HEARING BEFORE THE COMM. ON WAYS AND MEANS ON NOVEMBER 17, 1983, at 15 (Comm. Print 1983). The rate of unemployment must be at least 1.5 times the national unemployment rate. The legislation, however, does not define the terms "pervasive poverty, unemployment and general distress" as used in the legislation. *House Hearings, supra* note 80, at 14 (statement by Martin D. Levine, Deputy Assistant Director for Education, Employment, Housing and Community Development, Congressional Budget Office).

86. *House Hearings, supra* note 80, at 3 (statement by Congressman Jack Kemp stressing that the Enterprise Zone is designed to complement whatever the local government can offer).

87. *Senate Hearings, supra* note 80, at 75 (statement by Senator John H. Chafee). States have had enterprise zones for a longer period of time. Connecticut created an enterprise zone in 1981, followed by Arkansas and Illinois. Eleven zones have been established so far, and more states are considering similar legislation. OCU SCHOOL OF LAW & LINCOLN INSTITUTE OF LAND POLICY, E.Z. GAZETTE, Fall 1983.

Although the overall goal of state programs is to stimulate private sector investment in central cities, the means adopted are different.<sup>88</sup> The bill would allow the Secretary of HUD to revoke the enterprise zone benefits when local governments do not comply with the requirements.<sup>89</sup> Some suggest, however, that the governments of designated zones whose benefits are about to be revoked, should at least be notified and given an opportunity to amend their policies.<sup>90</sup> Once a firm locates in a designated zone and meets the minimum requirements, it would automatically be entitled to the benefits of the scheme.<sup>91</sup> The success of the program would depend not only on federal measures but also on state and local government contributions through their own tax relief measures.<sup>92</sup> The federal package is thus designed to complement local measures. For an area to be designated an enterprise zone for federal purposes, the state and local governments would have to pledge specific actions to reduce "the various burdens borne by employers and employees in such area."<sup>93</sup>

The legislation seeks to offer every incentive to encourage business to remain and to expand in distressed areas. "Making tax incentives available to all businesses in an enterprise zone ensures the most economically efficient expansion of business activity and job creation in economically distressed areas."<sup>94</sup>

88. *Id.* at 4-5 (1983). The most recent report on state enterprise zones demonstrates wide variation in the criteria chosen to designate a zone and in the incentives provided. The means to encourage redevelopment are also different. Tax exemptions cover sales and use taxes, franchise license taxes, or are fixed at a certain rate. To qualify as a distressed area in some states, a locality must show significant social problems; in others, it must show a loss of population or a percentage of welfare recipients. There is no uniform state enterprise zone legislation.

Another recent report concludes that these enterprise zone programs "have given a promising start to a new economic development initiative. In establishing a "climate of opportunity" for businesses and residents alike, local and state officials have pointed the way to a more effective national approach to resolving a pressing problem." R. COWDEN & G. BONETTO, ENTERPRISE ZONE ACTIVITY IN THE STATES 4-5 (Sabre Foundation, Nov. 1983). The new jobs have benefited the long-term unemployed, and new projects have had a great impact on the manufacturing sector. (29 percent of the total economic activity in these zones consists of manufacturing activities as opposed to 21 percent economy-wide). The states offer various tax relief incentives but the report stresses that more important are the streamlining of regulatory procedures and efforts to clean up the area are more important. The report also projected that the Treasury Department overestimated revenue losses from the tax incentives granted in the zones. Estimated at one billion dollars, the loss would, however, be partly compensated by gains based on sales taxes from the goods produced. Furthermore, the Foundation expects a number of failures of new businesses which will prevent initial business losses from being carried over to later tax years and weighing on Treasury receipts. In other words, new businesses may not cause any tax expenditure.

89. H.R. 1955, *supra* note 75, at § 101(a) (I.R.C. § 7871 (b)(2)).

90. *Senate Hearings, supra* note 80, at 208 (statement on behalf of the National League of Cities).

91. *Id.* at 394, 403 (statement of the National Council for Urban Economic Development). Earlier proposals set a threshold percentage for hiring new and disadvantaged workers in order to meet the enterprise zone requirements. Removing this criterion weakens the effective creation of new jobs.

92. *Id.* at 6 (statement by Marc Bendick, Jr.).

93. H.R. 1955, *supra* note 75, at § 101(a) (I.R.C. § 7871(d)(1)).

94. *Senate Hearings, supra* note 80, at 9 (statement by Donald T. Regan, Secretary of the Treasury).

### C. Tax Incentives Under the Proposal

Several tax benefits would be available under the proposed scheme. There are no provisions under present law for the federal income tax of an employer to vary according to the location of its employees.<sup>95</sup> Under the proposed scheme the employer in the zone would be eligible to claim a tax credit<sup>96</sup> covering the excess of present wages over the existing wages prior to the nomination, and an amount of the wages paid to disadvantaged workers.<sup>97</sup> Under the bill's scheme, an employee working in a zone could claim a nonrefundable tax credit of five percent of her qualified wages.<sup>98</sup> Historically, only certain low income families with children have been allowed an earned income credit.

The plan would grant a special investment tax credit for certain real and personal property in addition to the existing investment tax credit.<sup>99</sup> The basic credit would go toward depreciable tangible property, the special credit for property acquired and put in service for the period of the zone.<sup>100</sup>

Capital gains taxation would be eliminated for transactions involving property used for an enterprise zone trade or business as well as for transactions involving an interest in an enterprise zone "qualified business."<sup>101</sup> In other words, the gain from such transactions would not be treated as gain, provided certain enterprise zone requirements are met.

Property financed with tax-exempt bonds in an enterprise zone would not be restricted in recovering depreciation deductions.<sup>102</sup> Furthermore, although most small issue industrial revenue bonds will lose their tax-exempt status in 1986, owners of bonds issued by a municipality for the benefit of enterprise zone firms, would continue to be exempt from tax on the interest, reducing the cost of borrowing by the firm.<sup>103</sup>

The tax relief would reduce the amount of taxes paid by an employer, thereby

95. JOINT COMM. ON TAXATION, *supra* note 85, at 3.

96. H.R. 1955, *supra* note 75, at § 201 (I.R.C. § 44H). The federal income tax incentive provisions are under Title II of the bill. Credits for employers and employees is one of the principal provisions of the bill. *Id.*

97. JOINT COMM. ON TAXATION, *supra* note 85, at 19. In order to compute the employment credit, the qualified wages must be paid to qualified employees. A "qualified employee" is defined under § 201(f) as an individual whose services for the employer are related at least 90 percent to the employer's trade or business located in a zone, and who performs at least 50 percent of the services in the enterprise zone.

98. *Id.* at 24. The credit would phase out on the twenty-first anniversary of the enterprise zone designation. The term "qualified wages" represents all remuneration paid for the services of a qualified employee excluding any compensation from the government, up to one and one half times the wage base in effect for the purpose of the Federal Unemployment Tax Act.

99. *Id.* at 25.

100. H.R. 1955, *supra* note 75, at § 211 (I.R.C. § 48 (a)(1)). This additional credit is given to new construction as well as rehabilitation of buildings (three to five percent tax credit is allowed for personal property; ten percent for new real property).

101. H.R. 1955, *supra* note 75, at § 221 (I.R.C. § 1201(a)). The tax treatment for gain from sales of qualified treatment extends beyond the duration of the zone.

102. H.R. 1955, *supra* note 75 at § 231 (I.R.C. § 168 (f)(12)(C)).

103. JOINT COMM. ON TAXATION, *supra* note 85, at 31.



freeing up funds for capital investment and creation of new jobs.<sup>104</sup> The credit to employers for hiring new workers is intended to encourage on-the-job training.<sup>105</sup> Employees will also receive a tax credit designed to attract workers to the zone.<sup>106</sup> Capital gains exclusions are intended to stimulate investment in the zone by real estate developers and entrepreneurs starting new (especially small) businesses.<sup>107</sup> The Reagan Administration insists that these will be particularly successful because the program does not use subsidies and establishes no new bureaucracies. If no new business activity results, it presents no cost to the taxpayer (other than a revenue loss), as businesses already present in the zone take advantage of certain tax credits in the scheme.<sup>108</sup>

Regulatory relief is designed to ensure the rapid implementation of the enterprise zone program. Zoning and building permits would be expedited, land would be provided, and fire and police protection would be increased.<sup>109</sup> This relief would not apply to health and safety regulations, nor to laws prohibiting discrimination.<sup>110</sup> The local and state governments benefiting from an enterprise zone designation would be able to "petition for relief in their approved zones from any federal regulations not specifically required by the statute. For instance, regulations presently imposed by the Small Business Administration, the Internal Revenue Service, HUD, and the Commerce Department would be relaxed or waived."<sup>111</sup>

#### D. Criticism

Some critics of the enterprise zone plan consider it inadequate, since a lower tax structure by itself may not suffice to attract firms to an enterprise zone. Tax incentives, critics argue, are not the most efficient means of relieving the most serious constraints on business survival and growth in the inner city.<sup>112</sup> Opponents also point out that the legislation, as currently proposed, provides relief based on corporate income tax to businesses organized in the corporate form. Unincorporated businesses, however, perhaps more represented in distressed areas, do not receive assistance.<sup>113</sup>

104. *Id.* at 18. See Unger, *Enterprise Zone: Anglo-American Development*, 5 URB. L. & POL'Y 129, 144 (1982).

105. *House Hearings*, *supra* note 80, at 5 (statement by Donald T. Regan, Secretary of the Treasury).

106. S. BUTLER, *supra* note 14, at 139.

107. See generally *Reagan sends to Congress Message on Enterprise Zones*, 41 CONG. Q. WEEKLY REP. 634 (1983) (text of President Reagan's message to Congress on Enterprise Zones).

108. *House Hearings*, *supra* note 80, at 5 (statement by Donald T. Regan, Secretary of the Treasury).

109. *Senate Hearings*, *supra* note 80, at 77 (statement by Senator Arlen Specter).

110. *Id.* at 99 (statement by Samuel R. Pierce, Secretary of the Department of Housing and Urban Affairs).

111. *Id.* at 98.

112. *House Hearings*, *supra* note 80, at 5 (statement by Marc Bendick, Jr.) (suggesting that although the advocates of the zone see heavy taxation as reducing financial returns to work and to invest, taxation is only one of the factors contributing to high unemployment).

113. *Id.* at 11.

The National Council for Urban Economic Development has argued that tax incentives are not sufficient to attract investment in areas where other elements, such as trained workforce, suitable land, efficient infrastructure, and public services to assist development, are missing.<sup>114</sup> The National League of Cities, which also questions the tax relief approach, believes that the problems facing inner cities do not just lie in high taxes. The government needs to identify and respond to the particular problems each area faces.<sup>115</sup> The League and the United States Conference of Mayors, however, do not oppose the enterprise zone legislation in its entirety. The Conference, while supporting the ideas underlying the bill, believes start-up funds are imperative in helping new businesses and urges Congress to establish a "new venture fund." Furthermore, the program's tax credits are of greater benefit to larger firms than to smaller enterprises because the latter require more direct aid in the form of start-up funds. Tax deductions and credits will not help until the firm has been operating for some time.<sup>116</sup>

Several observers feel that the proposal's requirement of additional substantial concessions by states and their political subdivisions necessary in creating a zone, imposes unreasonable demands on already overburdened local governments.<sup>117</sup> The provisions of the bill would require local and state governments to forfeit revenues or increase services in order to encourage private businesses to take on investment risks that might not succeed.<sup>118</sup> It is not entirely clear whether the risk and time weighted rewards which the enterprise zone offers outweigh the costs or revenue losses. Competition among cities and states to attract corporate investment is already fierce.<sup>119</sup> The self-nomination process enshrined in the bill may further increase this competition. Smokestack chasing among cities that are already in decline indicates further that a package of tax incentives may not provide the best climate for economic development.<sup>120</sup>

The Reagan Administration believes that small businesses are the preferred means for economic growth in depressed areas, because they tend to generate

114. N.Y. Times, July 14, 1982, § 1, at 17, col. 5.

115. *Id.* The National League of Cities is more supportive of the Reagan Administration's views than is the Conference of Mayors. The former agrees with putting responsibilities back at the local level and relieving the federal government of some of its local programs. The fund would be used to promote development at the local level. N.Y. Times, July 14, 1982, § 1, at 17, col. 5.

116. Harrison, *The Politics and Economics of the Urban Enterprise Zone Proposal: A Critique*, 6 INT'L J. URB. & REG. RESEARCH 422, 425 (1982).

117. A study by a joint Congressional Economic Committee reveals that 50 percent of U.S. cities are spending more for operational expenses than they are collecting; recent federal cuts are exacerbating the financial difficulties the cities are undergoing and may drive them to the brink of collapse. N.Y. Times, May 17, 1981, § 1, at 1, col. 1. 118. H.R. 1955, *supra* note 75, at § 101 (a) (I.R.C. § 7871 (d)(2)).

119. See generally Kelly, *Corporate Prosperity and Urban Decline*, URB. CONCERNS, Feb.-Mar. 1980, reprinted in *Urban Revitalization and Industrial Policy: Hearings before the Subcomm. on the City of the House Comm. on Banking, Finance and Urban Affairs*, 96th Cong., 2d Sess. 364-71 (1980) (Kelly provides numerous examples of larger corporations that have bargained for lowered tax rates and more advantageous delivery of services in order to remain in town. Trying to compensate for a "bad business climate," local officials often have made major concessions to corporations.).

120. *Id.* at 369 (stressing that local government assistance, including tax breaks, low-cost financing, cheap land, and subsidization work forces, is an insignificant factor in affecting corporate location decisions).

more employment opportunities than large firms.<sup>121</sup> Moreover, small businesses tend to spend or reinvest their income locally rather than transfer it to shareholders in another region.<sup>122</sup>

There are, however, substantial disadvantages in using small businesses as the primary agent for redevelopment. Employment in small firms is precarious because their failure rates are high.<sup>123</sup> Small companies typically offer low wages and often overlook or are exempted from federal and local rules governing hiring, wage, and workplace policies.<sup>124</sup> They offer fewer opportunities for training in skilled areas and occupational advancement than do large firms. In light of these factors, small businesses should be seen not as a panacea to urban blight but as part of a broad spectrum of business forms generating job opportunities.<sup>125</sup> In the end, the enterprise zones may serve merely to induce relocation of businesses and skilled workers from areas subject to normal taxation, leading to large federal and local revenue losses. Such relocation would neither add to the total number of firms nor increase employment among residents of the zone.<sup>126</sup>

The American Federation of Labor and the Congress of Industrial Organizations (AFL-CIO) does not support the enterprise zone scheme.<sup>127</sup> The labor organization firmly rejects proposals intending to lower the minimum wage and to loosen laws regulating the workplace. Although such provisions were initially proposed, they have been deleted from the current draft of the enterprise zone plan. The union continues to reject the plan for what it terms a piecemeal approach and its inadequate substitution for a comprehensive reindustrialization program. The union believes that the scheme will result only in giveaways of badly needed public funds and wasteful competition for existing businesses without any net addition of jobs.<sup>128</sup> The AFL-CIO advocates an industrial policy that would set up a national industrial board to help revitalize the nation's sick industries and decaying communities.<sup>129</sup> Funds would be obtained through loans from a National Industrial Development Bank. Urban industrial investment is thus seen as part of a larger effort to revitalize American industries and realize full employment.<sup>130</sup>

121. For the Reagan Administration's endorsement of a study by D. Birch on the role of small firms in creating jobs in the economy, see *supra* note 50.

122. B. BLUESTONE & B. HARRISON, *supra* note 3, at 222.

123. Birch, *supra* note 50, at 7.

124. B. BLUESTONE & B. HARRISON, *supra* note 3, at 224.

125. *House Hearings*, *supra* note 80, at 15 (statement by Marc Bendick, Jr.).

126. *House Hearings*, *supra* note 80, at 1 (AFL-CIO Resolutions adopted at the Fifteenth Constitutional Convention in statement by Arnold Cantor, Assistant Director, Department of Economic Research, AFL-CIO).

127. AFL-CIO, Fact Sheet No. 25 (Mar. 5, 1982); Telephone interview with Steven Coplan, Legal Counsel of the AFL-CIO (Oct. 14, 1983).

128. Altman & Garten, *The Fallacy of Modern-Day R.F.C.*, N.Y. Times, Oct. 9, 1983, § 3 (Business), at 3 (urging Washington to bankroll the reindustrialization of the U.S. economy).

129. *House Hearings*, *supra* note 80, at 1 (AFL-CIO Resolutions adopted at the Fifteenth Constitutional Convention in statement by Arnold Cantor, Assistant Director, Department of Economic Research, AFL-CIO).

130. *Id.* at 2.

### III. CONCLUSION

Older urban areas, once the focus of industrial development, are by and large decaying. As a tool of urban industrial policy, the enterprise zone legislation attempts to remedy acute problems of industrial decline by encouraging businesses to reinvest and bring jobs to the unemployed. Through the enterprise zone proposal, the Tory Government offers and the Reagan Administration would offer incentives to stimulate investment in the inner cities, but at the same time reduce their overall commitment to local areas. The Tory Government has at least attempted to designate enterprise zones in areas already receiving government assistance. The scope of the British legislation is more specific than its U.S. counterpart. U.S. policy makers should examine the effectiveness of the British attempt to integrate enterprise zones in larger redevelopment programs. The U.S. has not yet shown how the enterprise zone bill would complement other urban aid programs to reduce the decline of inner city communities.

Implementing the Reagan Administration's enterprise zone legislation would be straightforward: firms would need only to locate within set boundaries to benefit from tax breaks. Firms would not need to meet any other requirements, such as growth targets or creation of training facilities. The primary objective is to realize business investment, regardless of the amount, based on the assumption that new businesses create new jobs. The program represents a new experiment in economic development. It would test whether a package of tax incentives can lead to urban revitalization.

The proposal, however, presents significant difficulties. These tax incentives may not be the right type of catalyst to transform decayed neighborhoods into places where industries will locate. Instead, they may lead to large revenue losses with no concomitant gain. Yet, communities in which these enterprise zones would be located have also experienced severe decline in areas such as services and housing stock. The proposed legislation does not address these issues.

Furthermore, the U.S. proposal focuses on small businesses as a means to create jobs, whereas the British proposal is not so narrowly tailored. Economic recovery is gaining new momentum, and businesses may seek new opportunities and new workers. The influence of small businesses on the national economy, however, is too uncertain to ensure continued growth in employment.<sup>131</sup>

131. The discussions on the role of the small firms versus large firms in creating jobs in the economy raises conflicting analyses. Birch states that assisting large firms has a long history of not working and claims that smaller businesses do not want direct assistance. Birch, *supra* note 50, at 11. *Contra House Hearings, supra* note 80, at 3-4 Congressman Jack Kemp, a proponent of the bill, states that federal assistance in fact cannot reach small businesses. These businesses often fail, which is embarrassing to federal agencies).