STATE ECONOMIC DEVELOPMENT POLICY: STRATEGIC APPROACHES FOR THE FUTURE

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I
THE GROWING STATE ROLE IN ECONOMIC DEVELOPMENT POLICY

Joseph Schumpeter characterized economic development in free-market economies as "creative destruction," a process by which old industries, jobs, and social patterns are constantly eroded and new ones are continuously born.[1] This pattern of development has emerged forcefully in the past several years in the United States. At the national level, it has sparked debate over how to restore national economic health and create a firm basis for future prosperity. This debate centers on economic arguments concerning how public policy can influence the development of a market economy.[2]

Although this debate has commanded a great deal of attention on a national level, it has obscured the major arena in which these issues are addressed: state and local governments and regional economies. While national initiatives in economic policy remain paralyzed by indecision,[3] an array of state economic development policies has been developed.[4] An example of this state/national dichotomy is manifested in the Reagan administration's urban enterprise zone proposal. Heralded as the supply-side approach to urban economic problems, the proposal has been immobilized in Congress for almost five years. In contrast, 23 states have instituted some type of enterprise zone policy,[5] and others are considering such legislation.[6] A proposal from the

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1. *See generally* J. SHUMPETER, CAPITALISM, SOCIALISM, AND DEMOCRACY (1942).

2. For a wide range of views, *see* TOWARD A NEW U.S. INDUSTRIAL POLICY? (M. Wachter & C. Wachter eds. 1981).

3. Herbers, *The States Learn to Rely on Their Own Resources*, N.Y. Times, Oct. 13, 1985 at E4, col.3.

4. Herzik, *Governors and Issues: A Typology of Concerns*, 56 ST. GOV'T 58 (1983); *see generally* D. Arnold, Gubernatorial Management of State Economic Development Policy (paper presented at the annual meeting of the Association for Public Policy and Management, 1984).

5. Herbers, *Local Incentives Draw Industry to Poorer Zones*, N.Y. Times, July 28, 1985, at A24, col.1.

6. *See generally* McGahey, *Whatever Happened to Enterprise Zones?* 7 N.Y. AFF., No. 4, at 45 (1983).

other end of the federal policy spectrum, the Reconstruction Finance Corporation ("RFC"), has not advanced far on a national level, either.[7] However, several states have experimented with publicly-financed investment banks or mini-RFCs.[8]

Experimentation by states is an historic feature of American social policy.[9] Unlike regional authorities in other capitalist countries, U.S. state governments enjoy a great deal of autonomy in the design and administration of taxation, commerce, and social welfare policies.[10]

Traditionally, federal socioeconomic policies have been cautious.[11] Proposals for income redistribution or overt governmental involvement in industry have been avoided in favor of programs offered as temporary solutions or integrated into the private sector.[12] Social Security, the most successful federal income redistribution program, is still viewed as an insurance fund that pays individuals from personal accounts. In reality it transfers income from current wage earners to retired persons and has substantially lowered the rate of poverty among the elderly.[13]

Traditional state economic development efforts also exhibit this cautious pattern. Economic policy at the state level aims to lure branch plants of large, multistate manufacturing firms to a state through infrastructure development, tax breaks, and preferential financing techniques.[14] Such activity had been considered "industrial development," but now is often derisively labelled "smokestack chasing."[15] Recent state government attempts to attract the General Motors' Saturn plant show that such approaches are by no means moribund. The same approach can be seen in employment issues. State and federal policies have focused on education and training to prepare workers for the labor market, rather than focusing directly on job creation or other more interventionist policies.[16]

A. *What Do States Do? Can It Work?*

Almost all state policies are now examined with an eye to their potential

7. *Would Industrial Policy Help Small Business?*, BUS. WK., Feb. 6, 1984, at 72.

8. McGahey, *supra* note 6; *Would Industrial Policy, supra* note 7.

9. *See generally* Skocpol, *The Political Formation of the American Welfare State in Historical and Comparative Perspective*, 6 COMP. SOC. RES. 87 (1983).

10. Arnold, *supra* note 4, at 4.

11. *Id.*

12. *See generally* Heclo, The Political Foundations of Anti-Poverty Policy (paper presented at the Institute for Research on Poverty Conference on Poverty and Policy, Dec. 6-8, 1984).

13. Danziger, *Demographic Change, Government Transfers, and Income Distribution*, 100 MONTHLY LAB. REV. 7, 9 (1977).

14. *See generally* R. GOODMAN, THE LAST ENTREPRENEURS: AMERICA'S REGIONAL WARS FOR JOBS AND DOLLARS (1979).

15. R. VAUGHAN, R. POLLARD, & B. DYER, THE WEALTH OF STATES 42-43 (Council of State Policy and Planning Agencies, 1986).

16. *See* R. MCGAHEY & J. JEFFRIES, MINORITIES IN THE LABOR MARKET: TWENTY YEARS OF MISGUIDED POLICY 28-35 (1985).

contributions to economic development.[17] Do these policies have any effect on the problems they are designed to address? Many economists argue that, at best, states can achieve only temporary advantages. They may even cause harm by excessively intervening in market processes.[18]

Most economic studies provide only limited insight into these problems, because they examine only the impact of individual policies. Two recent studies, however, examine not merely individual policies, but the overall comparative impact of state policies. They conclude that state efforts have had little measurable impact on unemployment or wage levels thus far.[19] The authors of these studies, Luger and Hansen, find that, while specific policies can make a difference,[20] the overall mix of state policies often is ineffective. This finding suggests that the negative impact of some programs cancels out the positive impact of others. Luger finds states that rely on capital subsidies, tax incentives, post-secondary educational support, and industrial attraction programs may be "spending their resources unwisely."[21] Job training programs, he says, create more low-wage jobs and lower incomes in the process.[22]

B. The Challenge for the Future

Today's public officials are confronted with a dilemma. The limited research available suggests that state policies often have little or no measurable impact on economic development.[23] Yet officials are expected to devise policies which will generate such development. Unfortunately, state officials, unlike academic researchers, do not have the luxury of arguing that nothing they do will make any difference. Instead, they must focus on guiding economic policy into the future.

It is necessary to distinguish two broad types of governmental policies: traditional adaptive policies that respond to social distress created by cyclical economic forces, and strategic policies that help shape structural economic forces. Most American socioeconomic policy has been adaptive, largely shaped by the New Deal and Great Society eras.[24] Adaptive policy has three essential elements: aggregate demand management through fiscal and monetary policy; a social safety net in the form of transfer payments such as Social

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17. Herzik, *supra* note 4.

18. *See* White, *The Role of States in Promoting Economic Development: Should Competition to Attract New Investment Be Restricted?* 9 N.Y. AFF., No. 3, at 6 (1986).

19. *See* M. Luger, Explaining Differences in the Use and Effectiveness of States' Industrial Policies 16 (paper presented at the annual meeting of the Association for Public Policy Analysis and Management, Oct. 18, 1984); Hansen, The Effects of State Industrial Policies on Economic Growth 13 (paper presented at the annual meeting of The American Political Science Association, Aug. 30 - Sept. 2, 1984).

20. Luger, *supra* note 19, at 14; Hansen, *supra* note 19, at 13.

21. Luger, *supra* note 19, at 15.

22. *Id.* at 16.

23. *See generally* White, *supra* note 18; Luger, *supra* note 19.

24. A. MATUSOW, THE UNRAVELING OF AMERICA: A HISTORY OF LIBERALISM IN THE 1960S (1984); *see also* L. THUROW, THE ZERO SUM SOLUTION: BUILDING A WORLD-CLASS AMERICAN ECONOMY 18 (1985).

Security and unemployment insurance; and a commitment to formal equal access to opportunity, achieved through extended political rights, education, and training for the disadvantaged.[25]

Adaptive policies succeeded after World War II, when the American economy dominated world markets.[26] The New Deal policies relied primarily on Keynesian and monetary policies related to the business cycle.[27] Government resources were used to address problems generated by economic changes, such as unemployment or regional distress. But adaptive policies are unlikely to be successful in the future. America no longer enjoys automatic superiority in productivity and technology as it did in the 1950s and 1960s.[28] In addition, the American economy is now inexorably intertwined with a competitive world economy.[29]

Today, the states and the nation face structural economic changes. This paper distinguishes traditional "adaptive" policies, which respond to cyclical and market-generated economic problems and which rely on traditional passive policy instruments such as taxation, from "strategic" policies, which address long-term non-cyclical problems through direct investment or other forms of active intervention in the economy. Structural economic problems call for a strategic, interventionist approach to economic problems. Generalized macroeconomic growth, especially in its recent form fueled by unsustainable levels of deficit financing and military spending,[30] is increasingly less effective as a solution to the problems of distressed industries, regions, and workers. Of course, adaptive policies are still needed to address continuing cyclical problems. During economic downswings, when jobs are scarce, social welfare costs rise, and competitive pressures intensify, governments must develop adaptive methods to address these problems. But the paradox of rising national poverty at a time of record employment levels indicates the inadequacy of using only adaptive policies. Similarly, such policies have done little to reverse the developmental disparities between regional economies, both across the nation and within states.[31] Major shifts in the employment base have resulted in an uneven distribution of socioeconomic costs and benefits among regions and within the population.[32] National cyclical recovery alone has provided little assistance to workers who have lost jobs in formerly stable but now shrinking manufacturing industries, to farmers and other residents of

25. *See generally* L. THUROW, *supra* note 24; R. MCGAHEY & J. JEFFRIES, *supra* note 16, at 3-10.

26. L. THUROW, *supra* note 24, at 21.

27. *Id.* at 18.

28. *Id.* at 47.

29. *See generally* K. PHILLIPS, STAYING ON TOP: THE BUSINESS CASE FOR A NATIONAL INDUSTRIAL POLICY (1984).

30. *See generally* Heller, *The Public Policy Experience*, in THE CHANGING AMERICAN ECONOMY 16 (D. Obey & P. Sarbanes eds. 1986).

31. *See* Luger, *supra* note 19, at 15-16; A. MARKUSEN, PROFIT CYCLES, OLIGOPOLY, AND REGIONAL DEVELOPMENT chs. 12 & 13 (1985).

32. A. MARKUSEN, *supra* note 31.

impoverished and debt-burdened rural communities, or to city residents with long-term employment problems, such as blacks and latinos.[33]

In designing policies, states should continue to assist those in need with innovative adaptive policies, but should also devise new policies and redirect traditional programs to address structural problems. Just as purely redistributive policies will not create future prosperity, so economic growth alone will not solve the problems of social inequality. States have an unprecedented opportunity to advance simultaneously the goals of stable economic growth and socioeconomic equality. Public officials must not accept the false dichotomy which dictates pursuit of one of these goals at the expense of the other.

To achieve the dual goals of development and equality, state policy-makers will have to coordinate myriad existing state and local policies with future policies. Creating specific initiatives, even those that recognize the importance of structural factors, will do little good if the effects of one policy cancel out those of another. Adaptive and structural policies alike affect a variety of socioeconomic factors, including capital, labor, technology, education and training, and social welfare. Specific policies will have to be coordinated among government, business, labor, and community groups to produce an efficient and flexible overall strategy for the future.

The following sections address policy coordination in more detail. Specifically, section II addresses a variety of specific policy goals, including capital, technology, labor, and training, as well as more nontraditional economic goals such as improving education, housing, and the quality of life. Section III outlines potential informational, institutional, and political barriers to the effective development and implementation of new policies. Section IV discusses these policies in reference to the needs of specific states and their subregions, paying special attention to New York and Massachusetts. The paper concludes with a suggested approach for future policy development.

II
POLICY ALTERNATIVES

Although many states have a large and diversified economic base, they can no longer rely on automatic competitive advantages in national and world markets. The nation's manufacturing industries have been battered by declining productivity and international competition.[34] Some states currently enjoy a lead in specific service sectors, but technological, government regulatory, and market forces could easily erode that advantage. Some of the forces that affect state economies—the federal deficit, extraordinarily high real interest rates, the loss of manufacturing markets due to the high exchange rate of the dollar, the withdrawal of federal support for social spending—are beyond state control. But there are still many opportunities for states to craft policies that

33. *See* Wise, *The Forgotten Americans*, BUS. WK., Sept. 2, 1985, at 50.

34. *See* M. Wachter & C. Wachter, *supra* note 2; L. THUROW, *supra* note 24, chs. 2 & 3; Zysman, *The International Experience*, in D. Obey & P. Sarbanes, *supra* note 30, at 41.

will bring older public programs into alignment with the future needs of the industrial and service sectors.

A. *Adaptive and Strategic Policies*

The following sections describe adaptive and strategic policies that are critical to achieving the following broad goals:

(1) Investment and job growth, specifically, providing new capital, encouraging new technology and other production innovation, and fostering new jobs and businesses;

(2) Improved productivity, including more progressive labor relations policies, better job training policy, and greater emphasis on managerial and ownership issues; and

(3) A higher quality of life, addressing the costs of, the effectiveness of, and the evolving demand for health care, social welfare and family policy, education, decent housing, and public safety.

In general, adaptive policies hinge on taxation and regulation which either modify the costs and benefits of a particular economic activity, or provide funds for social programs not provided by the private sector. In contrast, strategic policies, while they may incorporate tax and regulatory policy, seek out the best policy tools to achieve desired social goals. A strategic policy approach does not suggest a blanket approach to problems. In some cases, existing adaptive policy may be adequate, while in others, new strategic efforts can be used to complement adaptive policies. Strategic policies either can replace inadequately designed adaptive approaches, or can address emerging problems that cannot be resolved through adaptive approaches. Strategic analyses may sometimes bring to light the inadequacy of policy development to address particular problems.

1. *Capital Investment and Job Growth*

This section addresses three major policy concerns: providing new investment capital, encouraging technology and other production innovation, and furthering the growth of new jobs and firms. The continuing national debate over how to restore productivity growth has come to focus on allegedly inadequate levels of private investment.[35] Both at the national and state levels, this debate has been translated into a call for reduced taxes on capital investment and personal income. The Reagan administration's Accelerated Cost Recovery System ("ACRS") reduced effective taxes on new capital investment almost to zero.[36] Yet capital investment as a total percentage of Gross National Product ("GNP") actually declined slightly.[37] In addition, the administration's large personal income tax cuts were accompanied by a slight decline

35. Friedman, *Financing Capital Formation in the 1980s: Issues for Public Policy*, in M. Wachter & C. Wachter, *supra* note 2, at 95-126.

36. L. THUROW, *supra* note 24, at 226-28.

37. *Id.* at 207.

in personal savings.[38]

The single-minded focus on taxation as the solution to inadequate investment is a classic example of over-reliance on an adaptive policy. States have relied too heavily on tax-exempt investment funds from industrial revenue bonds and other sources to lure branch plants of large firms into the state as well as to provide for investment in resident firms.[39] Likewise, state and local governments have concentrated on tax relief through abatements of corporate income and property taxes for economic development purposes, along with more conventional reductions in personal income, property, and sales taxes.[40] Overall, the tax structure has come to be the single major policy tool that governments use in their attempts to preserve the investment capital of new and existing firms.[41]

But does taxation play such a powerful role in the location and composition of economic activity? Although states and localities rely heavily on taxation policy, a recent review of the effects of state and local taxes on location found that "[i]t would be absurd for governors to act on the conviction that location is entirely indifferent to state-local taxes, but equally absurd for them to accept the proposition that there is usually a big bang for the buck."[42] That paper does not address the possibility of achieving economic development goals through taxation policy, but instead argues that tax reformers must identify the "conditions in which strategic tax actions can have a strong impact" on economic development.[43] These actions include reducing taxes on regulated industries like utilities and railroads, eliminating intermediate purchases of goods and services from sales taxes, making property tax assessments more uniform, and substituting state value-added taxes for corporate income taxes.[44]

Legislators and governors often use tax policy to give relief to specific industries, allegedly because of the special and difficult conditions faced by them.[45] Some states also use tax credits for, or the concentration of tax-exempt bond funds on particular industries to encourage research and development of new technologies and job development.[46] In general, however, the measurable economic effects of such tax modifications are not significant,[47]

38. *Id.*

39. R. GOODMAN, *supra* note 14; Mead, *Resources for State Development: The Reform of Federal-State Development Programs*, 9 N.Y. AFF., No. 3, at 37, 58 (1986).

40. M. Luger, *supra* note 19.

41. R. GOODMAN, *supra* note 14.

42. Netzer, *State Tax Policy and Economic Development: What Should Governors Do When Economists Tell Them That Nothing Works?*, 9 N.Y. AFF., No. 3, at 19, 20 (1986).

43. *Id.*

44. *Id.* at 30-33.

45. R. GOODMAN, *supra* note 14.

46. M. Luger, *supra* note 19.

47. *See* Vaughan, *State Taxation and Economic Development*, in STATE TAXATION POLICY (M. Barker ed. 1979); *See* M. KIESCHNICK, TAXES AND GROWTH: BUSINESS INCENTIVES AND ECONOMIC DEVELOPMENT (11 Studies in Development Policy, Council of State Planning Agencies, 1981).

and are difficult to isolate and observe. The government is thus in the position of being unable to evaluate whether or not the goals of its particular tax policy are being met. States might do better to target particular firms, industries, and economic activities through more direct and specific strategic mechanisms.

Changes in taxation are, of course, far from trivial. Many states have taken steps to simplify the personal and property tax scheme, and have also moved towards sounder accounting and borrowing practices which can save money in borrowing costs.[48] Such efforts to stabilize the tax and revenue structure create a more predictable tax climate. But such changes do not obviate the need for an adequate strategy for obtaining new sources of investment capital, technological improvements, and new firms and jobs.

a. Providing New Investment Capital

Nationally, the net savings rate (a rough indicator of the available capital pool) fell to -2.5 percent of the GNP in the first four years of the Reagan administration.[49] Those funds are increasingly absorbed by the demands of the federal deficit; by the financing of the recent wave of mergers, acquisitions, and takeover battles; by aggressive lending by financial institutions with low profitability; and by the rapid build-up of short-term corporate and consumer debt.[50]

Policy makers facing the prospect of tight capital markets for the foreseeable future will have to explore new avenues for making capital funds available. Two innovative proposals in New York, based on state deregulation of financial institutions, creatively use traditional market mechanisms to achieve a structural goal: developing new pools of investment funds. First, the Temporary State Commission on Banking, Insurance, and Financial Services recently recommended that state banks establish a secondary market for small business loans, and invest state pension funds in long-term certificates of deposit with banks that agree to make long-term loans to small businesses in the state.[51] A second regulatory change allows state-chartered banks expanded real estate powers in return for developing $1 billion in new loans to low and middle-income communities.[52]

Restructuring financial institutions is not the only way to develop new sources of investment capital. One of the fastest-growing pools of capital in the United States comes from pension fund contributions made by employers and workers.[53] At the start of 1983, private and public pension funds amounted to $850 billion.[54] Organizations within states, and state govern-

48. M. KIESCHNICK, *supra* note 47.
49. L. THUROW, *supra* note 24, at 209.
50. *Id.* at 18.
51. Webb, *Financial Deregulation: What Can States Do?* 7 WAYS & MEANS 1, 1 (1984).
52. *Id.*
53. Litvak, *Pension Fund Investment and the Allocation of Long-Term Capital,* 5 ENTREPRENEURIAL ECON. 1, 2 (1983).
54. *Id.*

ments themselves, should develop new uses for relatively untapped sources of capital.

b. Technology and Innovation

Policy makers in many states have become enamored of so-called "high-tech" industries, and have encouraged their development and location within their states. The mechanisms are the familiar adaptive ones: developing high-tech industrial parks, granting special tax incentives to high-tech firms located within the state, and allowing tax credits for research and innovation. Many policy makers seem to mistakenly believe that the development of high-technology products and firms will immediately create a significant number of new jobs. They fail to realize that young high-technology firms provide very few jobs and almost no production jobs. It takes many years for firms to develop marketable products, and only then do their employment bases expand. Even then, the capital-intensive nature of high-tech production diminishes their role in job creation. Moreover, even if the products are mass-produced, high-technology production processes are often easily transferrable or "footloose," allowing firms to move production operations overseas to areas of lower labor costs.[55]

Despite these disadvantages, high technology can be an important part of a state's development strategy; comprehensive technology policy should encourage existing firms to improve productivity by adopting proven technologies. A focus on acquiring less proven high technology for its own sake could obscure such potential gains. The needs of existing firms cannot be met by an exclusive reliance on esoteric and less proven technology.

States are developing three types of initiatives in technology policy. First, states provide support for research and development. Many states have set up programs for this purpose, including Pennsylvania's Ben Franklin Partnerships, Ohio's Thomas Alva Edison Partnership, Massachusetts' Centers for Excellence, and New York's Science and Technology Foundation.[56] All of these programs support a variety of research activities, many of which involve cooperative efforts between firms and universities. While such industry-university collaboration can benefit both entities, state officials must ensure that such programs, when established at universities, do not overpower the traditional, broad mission of the university, including basic scientific research.

Second, states invest in research and development of new technologies and products outside of university centers, often through earmarked capital funds. Connecticut's New Product Development Corporation provides risk

55. M. Luger, The States and High Tech Development: The Case of North Carolina (working paper from Duke University Institute of Policy Sciences and Public Affairs, 1985); A. MARKUSEN, *supra* note 31, ch. 9.

56. M. CLARKE, REVITALIZING STATE ECONOMIES: A REVIEW OF STATE ECONOMIC DEVELOPMENT POLICIES AND PROGRAMS 61-62 (report of the Washington National Governors' Association, 1986); TECHNOLOGY, INNOVATION, AND REGIONAL ECONOMIC DEVELOPMENT (Office of Technology Assessment, U.S. Congress, 1985).

capital to new firms in return for royalties from the sales of the firm's products.[57] Similar programs exist in other states, and many others are busily planning such programs.[58] Two important issues must be considered in making these investments: the amount of private funds leveraged by public investment, and the type and size of the payoff in relation to public investment. For example, New York's Corporation for Innovation Development requires a 3 to 1 match, and reportedly gets a 6 to 1 private/public leverage, with a mixture of debt and equity.[59]

Third, states are becoming involved in technology transfers, which some states foster through industrial extension services.[60] Although advanced technologies can help improve productivity in private firms, adopting such technologies may require technical assistance, capital financing, training in the use of new equipment, and planning to avoid disruption of existing work patterns and employment. Extension services and other means of technology transfer can provide such assistance and play an important role in spreading technology to older firms.

As with other state policies, the use of an industrial extension services requires careful design if it is to assist the state in coping with potential structural problems. Many state technology programs concentrate on esoteric, cutting-edge technology, often ignoring the needs of better-established industries. In general, states should avoid excessive investment in esoteric technologies at the expense of productivity improvements in existing industries. One reason for avoiding over-emphasis on cutting-edge technology is founded in the argument by some scholars that the future of manufacturing in the United States rests with small, flexible, market-responsive manufacturing firms, since large-scale standardized production cannot compete with low-cost third world production.[61] Transfer of accessible, pragmatic technology will help develop such flexible manufacturing. A second reason for de-emphasizing esoteric technology is that it may distract policy makers from the human side of the production process and the fears of workers that technological innovation will mean job displacement. Therefore, a state industrial innovation extension service should establish close links with management, workers, and human relations experts and should not become dominated by engineering concerns.

Another problem with developing successful technology policies is the difficulty in assessing their impact. A major report by the National Science Foundation's Productivity Improvement Research Section found that significant technical innovations are bound up with the dynamics of organizational

57. Ioannou, *States Move to Stake Entrepreneurs*, 7 VENTURE 60-69 (1985).

58. M. CLARKE, *supra* note 56; TECHNOLOGY, INNOVATION, AND REGIONAL ECONOMIC DEVELOPMENT *supra* note 43.

59. NEW YORK STATE SCIENCE AND TECHNOLOGY FOUNDATION, 1985-86 ANNUAL REPORT, at 8.

60. *See generally* Haimson, *Why New York Needs an Industrial Extension Service*, 9 N.Y. AFF., No. 1, at 18 (1985).

61. M. PIORE & C. SABEL, THE SECOND INDUSTRIAL DIVIDE 221-50 (1984).

behavior.[62] Specific adaptations take years to work through, and thus the impact of traditional government policies regarding contracts, grants, regulations, and tax incentives cannot be evaluated easily.[63]

As with tax policies towards capital, states should develop explicit goals for technology transfer policy, goals that can be measured and evaluated when designing and assessing the policy.

C. *The Growth of New Jobs and Firms*

In recent years, state governments have concentrated on fostering new small businesses, in part because of claims that new small businesses create a disproportionate number of new jobs.[64] However, recent studies cast doubt on these findings.[65] As with taxation and technology policy, documenting the impact of indirect expenditure policies such as those aimed at promoting small businesses is problematic.

Another popular approach involves the use of tax-exempt financing raised through industrial revenue bonds ("IRBs"), or the use of property, income, and sales tax abatements for new job creation. Although the rationale for IRBs and other tax exemptions and abatements is to lower the cost of capital to borrowers, a fair amount of the tax subsidy accrues to high-income bond holders as a windfall. Most estimates figure the windfall at around 25 to 30 percent.[66]

Like most adaptive policies, traditional efforts aimed at producing new jobs and firm growth have employed indirect mechanisms such as tax expenditures, provision of tax abatements and tax-exempt financing, rather than mechanisms which concentrate directly on job growth. The logical culmination of such policies has been the push for enterprise zones, which provide packages of tax savings and other regulatory relief for firms willing to locate or expand in economically troubled areas.[67] Although hailed as an innovation in urban policy, enterprise zones are merely a continuation of traditional adaptive policy. Their only innovative aspect is their geographic targeting; otherwise, they feature the same combination of tax offsets and emphasis on the creation of small businesses, and hold the same limited prospects for success. Most tax offset policies fail to resolve the central problem for small businesses: the lack of operating funds and capital.[68] Small firms cannot benefit from tax

62. L. TORNATZSKY & J. SCHNEIDER, THE PROCESS OF TECHNOLOGICAL INNOVATION: REPORT OF THE NATIONAL SCIENCE FOUNDATION 49-75 (1983).

63. *Id.* at 187-216.

64. *See, e.g.*, Birch, *Who Creates Jobs?*, 65 PUB. INTEREST 3, 7-8 (1981).

65. *See, e.g.*, Armington, *Sources of New Job Growth: A New Look at the Small Business Role*, 6 ECON. DEV. COMM. 1 (1982).

66. Mead, *supra* note 39.

67. The concept has become somewhat elastic; for example, the state of Kansas declared an entire town to be an enterprise zone, while Louisana created 411 zones covering over one-eighth of the state's population. McGahey, *supra* note 6, at 47-48.

68. *See generally*, U.S. SMALL BUSINESS ADMINISTRATION, THE STATE OF SMALL BUSINESS: A REPORT TO THE PRESIDENT ch. 4 (1985).

credits, since they frequently have no positive cash flow for the first several years of their existence.

A similar problem occurs with the use of wage subsidies for new job creation. Several analysts have proposed using wage subsidies to private employers as a means of creating new jobs, especially jobs for the hardest to employ.[69] But wage subsidies have a dismal track record, and present the same bleak picture presented by business tax incentives: little response by employers, little or no impact on the employment of distressed populations, and windfalls to those few firms which receive the subsidies.[70] At the federal level, the NAB-JOBS program,[71] the WIN tax credit,[72] and the private sector wage subsidy program under the Youth Incentive Entitlement Pilot Project ("YIEPP")[73] all showed very low levels of employer participation. The YIEPP program offered a six month, 100 percent wage subsidy for hiring disadvantaged youth, yet fewer than one in five employers approached participated in the program.[74] In 1984, a six-state wage subsidy experiment using welfare grant diversion resulted in a total of only 200 job placements.[75]

The problems with wage subsidies parallel the problems with tax credits. First, small firms and new businesses often do not have the positive cash flow necessary to take advantage of tax credits and wage subsidies.[76] Second, large, prosperous firms have stable labor markets and means of employee recruitment, so tax credits and short-term subsidies will not be advantageous to them.[77] Firms may take credits and subsidies as windfalls, but there is little evidence that these policies create substantial numbers of jobs, either in new or existing firms.

To encourage the development of new jobs and firms, especially in distressed areas, more innovative policies than tax credits and wage subsidies are required. Among the policies worth considering are well-coordinated incubator programs, state assistance in venture capital funding, and transfer spending from social welfare programs.[78] Many states have begun to use incubators, especially for high-tech development.[79] Incubator programs are analogous to traditional industrial parks. In such a program, the government will make property available to a private firm at a reduced cost. When the firm grows too large for the space provided, it will move out and be replaced

69. H. O'NEILL, CREATING OPPORTUNITY: REDUCING POVERTY THROUGH ECONOMIC DEVELOPMENT, 152-57 (Council of State Planning Agencies 1985).

70. *Id.*

71. R. MCGAHEY & J. JEFFRIES, *supra* note 16, at 28-35.

72. *Id.*

73. W. DIAZ, LINKING SCHOOL AND WORK FOR DISADVANTAGED YOUTHS: THE YIEPP DEMONSTRATION: FINAL IMPLEMENTATION REPORT 105 (Manpower Demonstration Research Corporation, 1982).

74. *Id.*

75. *Id.*; *See generally* H. O'NEILL, *supra* note 69.

76. U.S. SMALL BUSINESS ADMINISTRATION, *supra* note 68.

77. M. KIESCHNICK, *supra* note 47.

78. *Id.* ch. 5; H. O'NEILL, *supra* note 69, ch. 6.

79. M. CLARKE, *supra* note 56.

by a new startup. This kind of incubator program will help to reduce rental costs for startup firms, and may prompt agglomeration effects if firms in the incubator program are in similar sectors of industry.

State governments should establish procurement target programs to work in concert with the incubators. An effective urban incubator strategy would allow coordination of other services for new businesses, including new enterprises that will initially service the incubator itself (for example, security and pest control enterprises). Incubators could be located in enterprise zones if zone policies do not conflict with safety and equity goals.

In addition to the policies discussed above for generating new supplies of capital,[80] state programs should include actively targeting capital for new firms. Although states have begun to explore new venture capital programs, most of these have been restricted to high-technology firms.[81] These efforts provide models that could be expanded, either by dedicating new lines of funding, or by tapping sources such as pension funds. Targeted capital pools should aim at small, potentially high-growth firms that do not produce highly specialized products or services. Such firms are good targets because it is their youthfulness, not the production sector in which they operate, that simultaneously causes under-capitalization and provides high growth potential.

States should consider expanding venture capital funding, assuring that firms can obtain adequate leveraging and that the state will recoup benefits from the investment. The strategy of the private venture capital market, where venture capitalists identify promising market niches and direct research and funding support toward them rather than passively waiting for firms to develop, can be adapted by states. This strategy could be especially effective if directed toward industries from which states make large direct purchases, and toward developing industries with export potential. For example, due to state purchases of pollution control technology the pollution control industry has excellent domestic and international export potential. A combination of state-sponsored research, funding, and leverage from procurement policies could help new firms get started in the pollution control industry, such as in toxic waste disposal or mass transit equipment production. New firms in these areas could become an important source of jobs and exports in future years.

A third potential source of funds for new businesses is social welfare and transfer spending, which is presently a method used only rarely for this purpose. Most states yield little or no economic development return for their social welfare spending.[82] Recent initiatives in Europe and Canada provide creative transfer spending models that American states should explore. For example, the United Kingdom's Enterprise Allowance Scheme provides for a weekly allowance in lieu of unemployment compensation for unemployed

80. Webb, *supra* note 51.

81. U.S. SMALL BUSINESS ADMINISTRATION, STATE ACTIVITIES IN VENTURE CAPITAL, EARLY STAGE FINANCING, AND SECONDARY MARKETS (1984).

82. H. O'NEILL, *supra* note 69.

workers who are starting a new business.[83] France's *Chomeur Createur* (Unemployed Entrepreneur) program gives all citizens entitled to unemployment compensation or welfare benefits a lump sum payment for starting a new firm; workers in plants that shut down are encouraged to pool their benefits to start new companies.[84] The government of Halifax, Nova Scotia uses welfare payments to capitalize new profit-making businesses that employ welfare recipients, facilitating the transition to other private sector employment.[85] In New York, the Community Service Society of New York City has established an employee-owned home health care company that employs former welfare recipients, using foundation and other support to capitalize the firm.[86]

In contrast to traditional state programs, the programs suggested above harness revenue streams that have not been used in the past as sources of capital for new firms. In addition, these programs concentrate on direct job creation, unlike existing programs which attempt to foster the creation of new jobs through indirect adaptive policies as tax credits or wage subsidies.

2. *Workplace Management, Economic Dislocation, and the Role of Job Training*

State initiatives in economic development must take into account the problems and concerns of the workforce. General gains in productivity, in either new or existing industries and firms, will be achieved only through the participation and cooperation of the work force. No efforts to create equitable prosperity can succeed without adequate work force training and education.

a. *Improving Productivity — Managerial Practices and Labor Relations*

Recent analyses of America's declining economic position criticize prevailing management practices in private sector firms.[87] First, managers often concentrate on measuring short-term, bottom-line performance to the exclusion of longer term investments.[88] Second, adversarial relations between workers and their unions sometimes forestall productivity innovations and adaptation to changing economic circumstances.[89] In addition, productivity im-

83. Friedman, *The Safety Net as Ladder*, 2 ENTREPRENEURIAL ECON. 20 (1984).

84. *Id.*

85. Strickland, *HRDA Enterprise Ltd.: A Case Study in Productive Alternatives for Public Transfer Payments*, 1 THE ENTREPREN. ECON. No. 7, at 9, 10 (1983).

86. Surpin, *Enterprise Development and Worker Ownership: A Strategy for Community Economic Development*, 9 N.Y. AFF., No. 1, at 32 (1985).

87. *See generally* W. ABERNATHY, K. CLARK, & A. KANTROW, INDUSTRIAL RENAISSANCE: PRODUCING A COMPETITIVE FUTURE FOR AMERICA, (1983); J. KENDRICK, IMPROVING COMPANY PRODUCTIVITY (1984).

88. Wellons, *Competitiveness in the World Economy: The Role of the U.S. Financial System*, in U.S. COMPETITIVENESS IN THE WORLD ECONOMY 357-94 (B. Scott & G. Lodge eds. 1985).

89. *See generally* Piore, *Beyond Social Anarchy*, in D. Obey & P. Sarbanes, *supra* note 30, at 156-66.

provements that do not require extensive investments often are simply overlooked.[90]

Historically, public policy has been based on the assumption that the managers and owners of private sector firms are in the best position to adapt to market shifts. This country's economic performance after World War II seemed to lend credence to this assumption. Blessed with technological superiority and a lack of serious international competition, American firms expanded rapidly, both in the home market and overseas.[91] Collective bargaining arrangements allowed large industrial firms to pass along increased employee wage and benefit costs to consumers; unions refrained from direct involvement in managerial decisions in return for these increases.[92] The role of public policy was limited to taxation and regulatory practices and to refereeing labor-management relations.[93] As productivity began to decline in the 1970s, management practices were subjected to closer scrutiny. Many analysts believe that declines in productivity during the 1970s, especially in manufacturing, were in part caused by poor private sector management policies and by the rapid growth of corporate bureaucracies with excessive layers of management.[94]

For example, a 1982 study of the cost advantage enjoyed by Japanese automakers over American car manufacturers found that only 25 percent of the Japanese cost advantage could be explained by higher U.S. employee wages and fringe benefits.[95] Another 8 percent was ascribed to labor-management friction in production. Most of the remaining differential was ascribed to superior Japanese managerial practices, including more efficient production technology (3 percent), "just-in-time" inventory methods (25 percent), more efficient management organization, and fewer white-collar workers and managerial layers (39 percent).[96]

Serious reforms of managerial and production practices are called for if American firms are to survive, compete, and prosper. Workers must be given a larger stake and a greater voice in firm's operations and production practices. Although many changes will necessarily come from within firms and labor organizations, states can foster and encourage such changes in a number of ways. For example, states should encourage improved workplace relations through quality of work life ("QWL") policies advocated and disseminated by governments and universities. New York State has begun such a program in conjunction with Cornell University,[97] but many more initiatives are needed in

90. J. KENDRICK, *supra* note 87, ch. 11.

91. L. THUROW, *supra* note 24.

92. *See generally* Piore, *supra* note 89.

93. *Id.*

94. J. KENDRICK *supra* note 87; Weining, *Managing Better*, in D. Obey & P. Sarbanes, *supra* note 30, at 203.

95. Holusha, *The Japanese Leadership Among Car Makers Facing Tests Abroad*, N.Y. Times, Apr. 1, 1983, at A-1, col. 1.

96. *Id.*

97. *See, e.g.*, Programs for Employment and Workplace Systems ("PEWS"), Avoiding

this area. Managers should be urged to encourage information sharing, joint decision making, job rotation, and labor participation in job design.

QWL programs, however, cannot supplant the role of labor unions and collective bargaining practices. If workers are to assume a role in improving a firm's productivity, managers cannot be perceived as using QWL programs to undercut employee rights. Any extensive state QWL program should be jointly developed by labor and management representatives. State universities could provide a forum for bringing these groups together. The expertise of business school faculties, industrial and organization scholars, and engineers could also be tapped in this way.

A second way to increase worker concern with firm productivity is to give workers and management a greater financial stake in the long-term health of the enterprise. There are a number of ways to achieve this goal. Pay structures can be tied to overall firm productivity.[98] A bonus scheme for all employees can be pegged to increases in value-added production. Greater job security can be offered in return for flexible wages and benefits.

These arrangements are preferable to profit sharing or output-based piece rate schemes. Emphasizing job security would lessen workers' legitimate concerns over their economic futures. Such emphasis should be a part of new technical innovation programs, giving workers an incentive to cooperate in raising productivity without fearing job loss. States can encourage the development of these programs by bringing together management, workers, and experts to formulate policy and by aggressively promoting these programs when they are consistent with the basic rights of employees.

Worker equity-participation programs (also known as employee stock ownership programs, or ESOPs) and worker-owned cooperatives can also increase productivity.[99] Several states financially support revolving loan funds from which workers borrow capital necessary to implement their own cooperatives.[100] In addition, both ESOPs and cooperatives enjoy substantial federal tax advantages.[101] In New York City and elsewhere, analysts view worker-owned enterprises as aiding the economic revitalization of poor urban areas.[102]

b. Economic Dislocation — Aiding Troubled Industries and Dislocated Workers

A critical issue confronting many states is the dramatic decline in manu-

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Plant Closings in New York State: An Integrated Approach (New York State School of Industrial and Labor Relations, Cornell University, July, 1986).

98. *See generally* M. WEITZMAN, THE SHARE ECONOMY: CONQUERING STAGFLATION (1984).

99. *See generally* Rosen, *Employee Ownership: A New Strategy for Economic Development*, 15 N.Y.U. REV. L. & SOC. CHANGE 1 (1987); *ESOPs: Revolution or Ripoff?*, BUS. WK., Apr. 5, 1985, at 94.

100. Henze, *ICA Revolving Loan Fund for Worker Co-ops*, 3 ENTREPRENEURIAL ECON. 6, 7-8 (1984).

101. Rosen, *supra* note 99.

102. Surpin, *supra* note 86.

facturing. Global shifts in industrial structure, accelerated by an overvalued U.S. dollar, have placed severe pressures on the manufacturing sector.[103] In 1983, the AFL-CIO estimated that over 215,000 workers lost their jobs because of plant closings.[104] Many displaced workers find jobs only after long searches, and then often at substantially lower wages.[105] Moreover, although declines in the number of manufacturing jobs have captured attention recently, the pressures of national and international competition, technical change, and sectoral economic shifts will affect employees in service industries as well. Some national projections of service sector employment, especially in clerical and other labor-intensive areas, predict a decrease in the demand for workers.[106]

Traditional adaptive responses to the problem of economic dislocation and disinvestment have included retraining or relocating dislocated workers and federal trade adjustment insurance.[107] These established responses should be supplemented with strategic policies that anticipate economic dislocation problems and develop programs that offer concrete solutions. One approach under study at state and federal levels would require private firms to notify authorities of economic problems that might result in layoffs.[108] Several states have developed emergency response systems that offer training assistance and other support when plants close.[109] For instance, Massachusetts provides extended health care benefits for workers who lose their jobs due to a shutdown.[110] Although such programs might be deemed inequitable because they fail to address the health care needs of workers who lose their jobs for reasons other than closings, the goal of having policies in place that facilitate quick response is an important one. Some states encourage cooperation by linking employers' receipts of state economic assistance to their willingness to participate in prenotification programs.[111]

But merely instituting mechanisms to respond to shutdowns and dislocations is not adequate policy standing alone. Strategic policy should incorporate more active approaches. One promising program model is Massachusetts'

103. L. THUROW, *supra* note 24, at 95-101.

104. *Worker Dislocation, Capital Flight and Plant Closings: Hearing on H.R. 2847 Before the Subcomm. on Labor-Management Relations of the House Comm. on Education and Labor*, 98th Cong., 2d Sess. 102 (1984) (statement of Marc Stepp, Vice-President, International Union, UAW).

105. LeGrande, *Economic Growth and Changing Labor Markets: Dislocated Workers: An Analysis*, CONG. RES. SERVICE 22 (Library of Congress, Dec. 1983).

106. *See* 9 to 5, The National Association of Working Women, Hidden Victims: Clerical Women, Automation, and the Changing Economy 9 (Sept. 1985)(unpublished report).

107. R. MCGAHEY & J. JEFFRIES *supra* note 16, at 42-44; M. CLARKE *supra* note 56, ch. 7.

108. A. MARKUSEN *supra* note 31, ch. 13; J. GORDUS, P. JARLEY, & L. FERMAN, PLANT CLOSINGS AND ECONOMIC DISLOCATION chs. 3 & 7 (1981).

109. M. CLARKE, *supra* note 56, ch. 7.

110. *Id.* at 95-97.

111. *Id.* ch. 7.

Industrial Services Program ("ISP").[112] ISP aids firms and industries in danger of shutdowns or major workforce reductions by providing financial and consultant services. Financial assistance is provided through a loan and investment fund and may even include credit for worker buyouts of firms. Consultant services include reemployment assistance and retraining programs for workers who are displaced by closings and personnel reductions.

C. *Training Policy*

The past 25 years of federal labor market policy reflect the belief that training is the key to solving employment problems. The Area Redevelopment Act of 1962, the Manpower Development and Training Act, War on Poverty programs such as CETA, and the Reagan administration's Job Training Partnership Act ("JTPA") are all premised on a view of the labor market that ascribes most employment problems to inadequate skills and education among unemployed people.[113]

The "skills mismatch" hypothesis, along with the organizational changes and funding cutbacks introduced under JTPA, largely determine most state policies.[114] Many current state efforts include extensions of previous CETA programs, with very little change except for a reduction in scale due to the decrease in available federal funding. Although training and retraining efforts continue to be an important component of socioeconomic policy, there is reason to question the "mismatch" hypothesis as a sufficient explanation for employment problems, and as the basis for future training policy.

Training programs, by themselves do not directly address the issue of job creation and are not usually linked to direct job placement. Most training programs seek to teach workers skills applicable to private sector employment only. Occasionally, tax credits and other inducements are also offered to create temporary jobs in the private sector with the hope that permanent employment will result from increased levels of experience and training.[115] However, training approaches have not been adequately integrated with changes in the economy, nor have they targeted appropriate groups with sufficient accuracy.

One area of employment and training policy that continues to present difficulties is the issue of youth unemployment.[116] Adaptive policies do not seem to be assisting unemployed youth, especially disadvantaged minorities in inner cities. Calls for further tinkering with the wage structure, such as the introduction of a subminimum wage for youth, are unlikely to make any dent in the problem. Youth programs that combine training and work opportunities with continued schooling are needed. Such programs can be combined

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112. *Id.* at 95-97.

113. *See* R. McGahey & J. Jeffries *supra* note 16, at 28-35.

114. *Id.*

115. H. O'Neill *supra* note 69, at 155.

116. *See generally* Rees, *An Essay on Youth Joblessness*, 24 J. Econ. Literature 613 (1986).

with local economic development efforts to create appropriate jobs for in-school youth: local, part-time employment, usually in retail trade. Although exposing youth to possible career alternatives may serve a useful educative function, most teenagers are not ready to settle on career choices.[117] Because youths' labor market goals are usually exploratory, youth training and employment policy should factor exploration into program design.

Adult training programs should differ from those for youth. New policies should concentrate on creating closer linkages between actual jobs and training. Two types of initiatives in particular should receive more attention: employer-specific training and industry-specific training. Employer-specific training links training with actual labor market conditions. Employer-specific programs must be carefully designed; too often, they fail to account for the changing nature of the labor market and the emerging needs of industries. State programs might better concentrate on industry-specific training, which develops clusters of skills applicable to a variety of jobs within a single industry. Industry-specific training is more generalized, has more curriculum continuity from year to year, and has more general utility to a variety of employers.

States should also explore the use of "first source" agreements, whereby firms that receive state economic aid pledge to use state referrals as their "first source" of new hires. In addition, several U.S. cities require private developers who receive public financing assistance to reciprocate by providing money or job services.[118]

The introduction of JTPA presents states with a variety of problems, but also some opportunities for innovation. Although JTPA reduces the level of funding substantially below that of the CETA program (federal funding for job training has fallen by over 40 percent in real dollars between 1978 and 1983),[119] it encourages more autonomy for states and localities and sets aside funds for experimental and innovative programs.[120]

JTPA funds and administrative practices must be better integrated with other economic development policies. Employer and industry-specific skill training and first source agreements are two means to that end. In addition, states should encourage more experimentation in training policy, by using both JTPA funds designated for that purpose and state funds.

Many program advances can come from simply providing better coordination and support for existing programs when they are effective for particular

117. *See generally* P. OSTERMAN, GETTING STARTED: THE YOUTH LABOR MARKET (1980).

118. Pickman, *Tapping Real Estate Markets to Address Housing Needs*, 9 N.Y. AFF., No. 1, at 3, 5 (1985).

119. Burtless, Public Spending for the Poor: Trends, Prospects, and Economic Limits, (paper presented at the Institute for Research on Poverty Conference on Poverty and Policy, Dec. 6-8, 1984).

120. G. WALKER, AN INDEPENDENT SECTOR ASSESSMENT OF THE JOB TRAINING PARTNERSHIP ACT. PHASE I: THE INITIAL TRANSACTION (1984).

populations. For example, Massachusetts' "ET Choice" approach [121] and extensions of the Supported Work Models developed by the Manpower Demonstration Research Corporation[122] both build on current policy options. ET Choice is aimed at moving welfare recipients into private sector jobs by helping them to design an individualized package of training, counseling, education, and other aids.[123] Supported work, which uses graduated exposure to private-sector work environments as a means of assisting AFDC[124] recipients and other hard-to-employ groups, is a more expensive proposition.[125] Both programs are superior to traditionally punitive "workfare," which brings about a short-term reduction in the welfare rolls with no real improvement in labor market opportunities for the disadvantaged.[126]

Despite the promise of these programs, training policy alone cannot create more and better jobs. Any new training initiatives must be closely aligned with policies for job growth.

3. *Quality of Life Factors*

Many issues other than those traditionally associated with economic development policy determine a state's economic future. The quality and expense of services such as health care, education, and housing are all critical to economic development. These "quality of life" factors may be more important in determining the location of new businesses and the expansion of existing ones such typically cited factors as business and personal taxation.[127] In addition, the jobs and income created by education, housing, and health care often produce multiplier effects in different regions of a state.

New Deal and Great Society adaptive policy approaches did not integrate public spending on quality of life issues into its basic economic framework. Adaptive policy emphasizes Keynesian aggregate demand management, monetary policy, and tax as the main instruments for fostering prosperity. Quality of life issues have been addressed when revenue was high, but conditions of macroeconomic stagnation in the 1970s and the increasing federal deficit in the 1980s have left policy in these areas erratic.

Underdeveloped policy on quality of life issues will be costly to businesses and workers in the future. States commit large sums of money in these areas without carefully integrating quality of life programs with more traditional economic development activities. Quality of life issues should not be subordinated to narrow economic concerns; rather, states should seek to coor-

121. Kuttner, *A Jobs Program that Deserves More Aid*, Boston Globe, Sept. 27, 1985, at A26.

122. H. O'NEILL, *supra* note 69, at 157-61.

123. *See generally* Anderson, *Developing Talent*, in D. Obey & P. Sarbanes, *supra* note 30, at 147-55.

124. H. O'NEILL *supra* note 69, 157-61.

125. Anderson, *supra* note 123; H. O'NEILL, *supra* note 69.

126. Anderson, *supra* note 123; H. O'NEILL, *supra* note 69, at 9-11.

127. *See generally* A. MARKUSEN *supra* note 31, chs. 12, 13.

dinate quality of life spending with overall socioeconomic goals. No area of public spending will be immune from such examination in the future. The spending, resource, and regulatory allocation patterns of the New Deal and Great Society are running out of steam, but merely relegating these social policies and the problems they address to allegedly efficient private market forces will not foster future economic or political stability.

a. Health Care

Health care expenditures rose from four percent to eleven percent of GNP between 1940 and 1983, with most of the increase occurring after 1960.[128] This change was mirrored in employment; according to some estimates, between 1960 and 1970, the health care sector provided more than one of every eight new jobs in the U.S. economy.[129] Tilly notes that these trends, backed by public and private policies, amounted to "an uncoordinated industrial policy" encouraging the growth of health care and the hospital industry.[130] Many of the new jobs created went to women and minorities.[131]

Recent cost containment measures at the federal level have merely slowed the rise in growth, although health care costs continue to rise faster than the general rate of inflation.[132] Health care costs are an increasingly important part of total compensation for many private sector businesses.[133] And the aging of the nation's population[134] will be accompanied by escalating demands for health care into the forseeable future.

The rapid rise in health care costs caught many policy makers unaware. As costs ballooned in the 1970s and as government revenues fell, policies focused on exercising tighter control on total expenditures.[135] Unfortunately, much of the cost saving seems to have come at the expense of the underinsured or uninsured poor and the working poor. Private insurance for health care has fallen over the last decade, partly due to the shift in employment away from manufacturing and other industries with high levels of insurance.[136] The United States remains the only major western capitalist economy that does not provide some form of universal or catastrophic health care insurance.[137]

128. C. Tilly, Industrial Policy, Growth, and Inequality in the Workforce: The Case of the Hospital Industry, 1945-1980, 1 (paper presented at The Association of Collegiate Schools of Planning Conference, 1984).

129. C. Tilly, *supra* note 128, at 2.

130. *Id.* at 3.

131. *Id.*

132. *Id.* at 9-10.

133. P. Starr, Health Care and the Poor: The Last Twenty Years 8 (1984) (unpublished paper presented at the Institute for Research on Poverty Conference, 1984); C. Tilly, *supra* note 128, at 3.

134. C. Ross, The Trend in Poverty, 1965-83: Tables from the Current Population Survey, Table 10 (paper prepared for The Institute for Research on Poverty Conference, 1983).

135. P. Starr, *supra* note 133, at 39; C. Tilly, *supra* note 128, at 10.

136. P. Starr, *supra* note 133, at 29-30.

137. *Id.* at 13, 60.

Market-oriented cost containment policies are not likely to solve the problem. In any case, current efforts continue the post-war health care policy "tilt" toward traditional, expensive providers.[138] Programs that do not address the structure of health care delivery will not correct this bias. As one analyst points out, "state programs that redistribute the cost of hospital care for the poor, but do nothing to redistribute the cost of other services, would simply repeat and extend" this tilt.[139]

It is likely that problems associated with the current system of insurance and the future of the health care and hospital industry will worsen in the future. Simply subsidizing health care providers, a typical adaptive approach, can no longer be viewed as an adequate solution. Traditional cross-subsidization policies that spread the tax on all consumers of health care tend to reinforce the existing set of spending patterns that have led to the current impasse. Expansion of Health Maintenance Organizations ("HMOs") and of preventive care, home health care and hospice facilities should be considered. Development of these alternatives would create a need for new, exportable products and new jobs, and thus prompt the development of new manufacturing industries within a state.

b. Education

Like health care, education is a major cost and a major resource for states. Education provides substantial levels of employment in all states, especially in some subregions. In addition, policies that envision the development and use of new technologies for maximum productivity will fail if workers are not adequately educated.

The same policy configuration that accelerated health care spending can also be seen in education. Pressures on public expenditures have led to slowing rates of educational spending.[140] At the state and local level, property tax revolts in California and Massachusetts put caps on local revenues that had been a major support of educational spending.[141] Public institutions' enrollment also shrank as cost pressures caused reductions in student loans and grants.[142] Not surprisingly, this spending constriction had its greatest impact on the poor and minorities. Black enrollment in American colleges and universities has fallen consistently over the past several years,[143] which could contribute to growing racial and class polarization in the future.

Declining enrollments will also constrict future economic performance.

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138. *Id.* at 57.

139. *Id.* at 57-58.

140. T. EDSALL, THE NEW POLITICS OF INEQUALITY 230 (1984); *See generally* Stiefel and Berne, *The Equity Effects of School Finance Reforms: A Methodological Critique and New Evidence*, 13 POL. SCI. 75 (1981).

141. Bridges, *Property Tax Reform*, in AMERICA'S CITIES AND COUNTIES: A CITIZENS' AGENDA, 1983-84, 67-71 (Conference on Alternative State and Local Policies, 1983).

142. Kolbert, *Minority Faculty: Bleak Future*, N.Y. Times, Aug. 18, 1985, at 42, col. 1.

143. *Id.*

For example, because over 40 percent of American Ph.D. candidates in science are foreign students, it is foreseeable that the pool of engineers and science teachers may become dangerously small.[144] Of course, some foreign students may opt to stay in the United States, but even the possibility of a constriction on the supply of scientific expertise is a major cause for concern. At the other end of the educational continuum, the traditionally disappointing performance of public elementary and secondary educational institutions[145] must be addressed if states are to develop an adequately educated labor force.

Prevailing state educational policy must be reformed at a fundamental level. The performance of public schools, especially in poor and minority communities, must be improved, possibly by providing higher compensation for professional teachers or by encouraging competent non-professionals (for example, recent college graduates and retirees) to enter the field. At the university level, states will have to coordinate the diffuse activities of their university systems, along with the multiple and sometimes competing programs of private universities. Programs should be reexamined, specialized, and consolidated. As with health care, simple cross-subsidization of the existing system probably will not improve the quality of education, and will leave the current inefficient policy structure intact.

c. *Housing*

In the post-World War II decades, subsidized low interest rates and infrastructure policy encouraged the construction of new housing. This construction boom provided jobs, increased incomes, and fostered new community development. Today, financing for housing must compete at higher market rates of return, while recent changes in tax policy under the Reagan administration have tilted investment incentives away from housing construction and toward construction of offices and shopping malls.[146] The high cost of housing in many regions makes it more difficult for many families to buy homes, and also influences the employment location and expansion decisions of private firms. Especially for low-income and indigent people, the supply of, and federal support for, affordable housing has declined dramatically.[147]

Simply restoring previous federal funding levels would not solve the housing problem. Some state and local governments are experimenting with leveraging public funds through regulatory changes or other practices.[148] Other states and local governments are experimenting with various forms of private developer commitments, for example, monetary contributions to housing trust funds or construction of housing for poor and low-income popula-

144. Botstein, *Nine Proposals to Improve Our Schools*, N.Y. Times, June 5, 1983, Sunday Magazine, at 61.

145. *Id.*

146. *See generally* A. DOWNS, NEIGHBORHOOD AND URBAN DEVELOPMENT (1981).

147. Zigas, *America's Low-Income Housing Crisis*, 4 ENTREPRENEURIAL ECON. 2 (1983).

148. Pickman, *supra* note 118.

tions.[149] Some analysts have recommended programs to tap the interest earned by existing real estate escrow accounts. These programs would provide badly needed housing capital.[150] Such innovative approaches merit exploration by state and local governments.

The housing regulation and taxation structures also require examination. The large stock of *in rem* housing held by older cities is a valuable asset. This housing could be turned over to community groups or others who will broker the conversion of this wasted stock into privately owned housing through "sweat equity" and other means.

States should also encourage housing conversions in cities, understanding that this may involve some displacement of existing residents. Currently, poor residents of urban areas cannot make substantial capital investments in their housing. States which are not prepared to provide massive levels of investment, yet also refuse to allow private investment in poor urban areas, have in effect adopted a policy of slum preservation.[151] It would be better for states to permit new investment. Investment could be coupled with programs designed to facilitate relocation of affected residents, set-asides of some new housing for the poor, and contributions to funds for new housing. Building codes also should be reexamined and relaxed where consistent with public safety.[152]

Housing trust funds can be developed with the participation and leadership of non-profit and community institutions, such as churches and foundations. The Nehemiah Plan in Brooklyn, New York, coordinated by the Brooklyn Archdiocese, has sponsored the growth of a large number of new housing units for families in Brownsville, a poor area where no new housing has been built for many years.[153] State and local governments should actively support religious and community groups in such efforts by offering regulatory, legal, and financial assistance.

d. Families and Children

A final disturbing trend that demands the attention of state policy makers is the growing number of children living below the poverty line,[154] particularly black children.[155] In 1985, 22 percent of all children, and 48 percent of all black children in the United States lived in households with incomes below the poverty level, compared to 14 and 40, respectively, in 1969-1970.[156] More

149. *Id.* at 7-12.

150. Rosen, *Housing Trust Funds: How States Can Meet Low-Income Housing Needs*, 6 WAYS & MEANS 1, 5 (1983).

151. A. DOWNS, *supra* note 146, at 149.

152. *Id.* at 38.

153. Zukin, *Housing for the Working Poor: A Historical View of Jews and Blacks Living in Brownsville*, 9 N.Y. AFF., No. 2, at 3, 13 (1985).

154. Ross, *supra*, note 134.

155. BUREAU OF THE CENSUS, AMERICA'S BLACK POPULATION: A STATISTICAL VIEW, 1970-1982 4-9 (1983).

156. Malcolm, *New Generation of Poor Youths Emerges in the U.S.*, N.Y. Times, Oct. 20, 1985, at A1, col. 1.

than half of all poor children in the United States live in households headed by single women.[157] Pre-natal and post-natal care often is inadequate in these households, contributing to high infant mortality rates as well as health and disability problems later in life.[158] As New York Senator Daniel Moynihan has noted, "the U.S. today may be the first society in history where children are much worse off than adults."[159]

In addition to creative job development efforts in poor communities, states must study and improve family and child care policy. Adequate child care provisions would allow women to enter the paid labor force. Expanded employment among young minority males would facilitate the formation of stable, two-parent households. Particular attention should be paid to strengthening informal institutions among the urban poor. Traditional social welfare programs have been attacked by both the left and the right for undercutting the autonomy of the poor,[160] and new leadership on these problems must come from within the black and latino communities.

III
ORGANIZATIONAL AND INSTITUTIONAL ISSUES

Three organizational and institutional problems cut across all the policy initiatives suggested in this paper. First, there is the problem of lack of information for policy analysis. Often, state governments lack accurate information and fail to develop the capacity to assess the capital needs of existing and new firms, the training needs of the displaced and disadvantaged, and the transfer of production technologies to new firms.

Second, there is the related problem of agency coordination. Bureaucratic fragmentation makes implementing coordinated strategic policy difficult. Programs that might aid in strategic policy are scattered among commerce, labor, finance, and education departments. In addition, many fragmented public authorities are further subdivided. This fragmentation is partly the result of New Deal and Great Society program structures. Many programs, such as industrial attraction strategies or traditional employment and training, were developed in the past to address the problems of the past. For example, training programs often are supervised by labor, education, and social welfare departments, while economic development efforts aimed at creating new jobs are administered by commerce and other business-oriented

157. Ross, *supra* note 134.

158. Malcolm, *supra* note 156, at A56, col. 1.

159. Interview with Senator Daniel Moynihan, *quoted in* Malcolm, *supra* note 156; Moynihan, Family and Nation (unpublished address by U.S. Sen. D. Moynihan presented as the Godkin Lectures at Harvard University, April 8, 1985; copies available from the office of Sen. Moynihan).

160. *See generally* F. PIVEN & R. CLOWARD, REGULATING THE POOR: THE FUNCTION OF PUBLIC WELFARE (1971); C. MURRAY, LOSING GROUND: AMERICAN SOCIAL POLICY, 1950-1980 (1984).

agencies.[161] The goal of linking training to economic development will be hard to meet without some degree of structural integration.

The third institutional problem is an extension of the second: how to ensure that new and existing state policy initiatives actually reach businesses, workers, and communities. New policy initiatives are unlikely to achieve their maximum potential without accurate information, policy analysis, institutional coordination among agencies, and effective outreach. In a period where state governments must make the most effective use of scarce resources, efficiency in these areas should be encouraged.

A. *Information for Policy Analysis*

Policy makers need accurate, timely information on a state's economy, industries, regions, labor force and programs to design and implement effective strategic policies. Unfortunately, central sources of data and information do not exist in most states,[162] although states routinely gather information on employment patterns, taxation, business and personal finances, program spending and participation, and the like. In addition, private sector sources develop credit reports and financial analysis of industries, firms, and local and state governments; and university researchers generate a multitude of studies that link these types of data and generate new primary information.

Unfortunately, none of these data are brought together in a useful way. Businesses do not have access to reliable information on economic conditions in different regions of states, making it more difficult to formulate strategy on locating, lending, and borrowing. Within state agencies, data on employment are not linked to data on businesses. Data gathered to report on individual program efforts are not organized to make them comparable with other data sources.[163] As a result, evaluating the effectiveness of any particular program is difficult.

Although lack of information has troubled state planners for many years,[164] little has been done to create more accurate and accessible information. States must provide for adequate information bases to take advantage of the gains yielded by other components of overall economic planning.

B. *Strategic Planning, Policy Analysis, and Program Coordination*

The second central problem that affects state economic development is the lack of coordination among different policies and programs. Programs and policies have been developed over time to address specific issues and needs. These policies must be reviewed and coordinated with an eye to improving efficiency. New strategic policies must be considered against the

161. McGahey, *State Economic Development in a Changing World Economy: Strategic Planning and Economic Extension Services*, 9 N.Y. AFF., No. 3, at 63, 74 (1986).
162. *Id.* at 73.
163. *Id.* at 74.
164. M. CLARKE, *supra* note 56, ch. 3.

backdrop of existing programs to avoid unnecessary duplication, inefficiency, or counterproductive efforts.

A state strategic planning office can act as a coordinator of policies.[165] Like strategic planning departments in the private sector, such an office can assess existing and proposed programs in light of future goals. The office could present an annual strategic plan that would describe in detail each existing program, its level of funding and source of support, its specific goals and targets, and how each program's mission fits into an overall economic development strategy.

There are two keys to the success of a strategic planning approach. First, the office must be able to use and evaluate accurate information. The information may be obtained in a variety of ways: from industry studies, input-output and econometric models, fiscal impact analyses, and specific policy analysis. Much of the research and assessment work could be contracted to existing research services within the state government and the universities; this coordination could eliminate some redundancy. Research and policy analysis resources can also be obtained from private sector firms and associations, labor unions, local governments, and community organizations.

Second, a strategic planning office must be backed by a strong, continuing executive interest. The governor's office must take the lead in supporting strategic planning, providing adequate resources and political support, and allowing full use of the planning. Piecemeal efforts will fall prey to existing bureaucracy and will confound any effort to design, implement, and evaluate policy.

C. Assessment and Outreach — Involving the Entire State

The final institutional challenge is that of mobilizing and coordinating all the state's resources for future economic growth and equality. Many states have large concentrations of independent expertise on economic and social issues. These resources need to be enlisted. This expertise can be useful in drafting policies, and in insuring that they are implemented effectively.

For example, many states have substantial concentrations of expertise within their banks and other financial institutions. Analysts in these industries routinely track particular industries, firms, technologies, and labor force patterns. States also have a substantial amount of private sector management and consulting expertise that can be used to design ways for the state to do business more efficiently. State public and private universities, non-profit institutions, labor unions, and community organizations share similar skills. State officials must tap this expertise by routinely having experts donate time and skills whenever possible. Experts need to be made aware of the specific needs of state officials. One possibility is for states to develop an information

165. McGahey, *supra*, note 161.

exchange and clearinghouse for economic and technological expertise and research.

These connections can play an important role in designing and implementing policies. Programs will be most effective if various groups and experts participate in their design at an early stage. The process of designing a venture capital program ought to include the collaboration of financial analysts and industry experts to determine such investment decisions as whether a state should target high technology firms or concentrate instead on general job growth. Training programs ought to draw upon the knowledge and experience of labor organizations, trade associations, industry and labor market analysts, and equipment manufacturers. These specialists are best equipped to answer the planners' questions: what skills will be needed in regional industries in the coming years? What educational institutions, private training programs, unions, and on-the-job training will best develop those skills? Planners of technology transfer programs need to develop expertise on these matters, while garnering support from workers and management, to ensure that threats to job security are minimized.

These may appear to be overly ambitious agendas. However, no new programs or expertise beyond what many states now possess or have access to would be required. Most states lack a coordinated partnership among government officials, private sector managers and analysts, union and labor experts, university researchers, and community groups and local government, along with strong executive-level interest and support. Providing the coordinated policy analyses or program responses discussed here would not require new agencies or substantial new levels of funding. They would require only strategic coordination and direction. Without this type of stategic planning, policy responses will be uncoordinated, wasting public resources and creating a poor environment for future economic growth and equity.

IV
New York and Massachusetts — Comparing State Strategies

Particular economic development policies and methods of policy organization ultimately come together, for better or worse, as a total state strategy in economic development. Many states share individual programs, but the totality of policy efforts seems to influence economic development more than any single policy. Each state develops what might be called a "policy style," partially determined by economic factors (industrial composition, regional economic variation, labor force issues) and partially by state political organization and culture (the powers of governors relative to legislatures, the history and style of policy making, the use of public authorities).

Policy styles can produce rather different overall programs in different states, even when the states share many of the same economic development goals and experiment with policies on many of the same issues. The wide variety of policies discussed in Section II of this paper gives some idea of the current range of experimentation. This section concentrates on how economic development policy is emerging in two states, New York and Massachusetts. Both states have Democratic governors who are very active on economic development issues. Both are in the northeastern region of the U.S., which suffered during recent recessions and is now undergoing something of an economic revival.[166] Both states have urban and rural populations, growing and declining industries, and varying regional economies. The differing policy styles that are emerging in these two states are worth examination.

A. Massachusetts: Industrial Policy in One State?

Massachusetts' innovative economic programs have received much national attention recently. This state's economic and social welfare initiatives are being developed at a time when Massachusetts has one of the lowest unemployment rates in the nation. The state's economic rebound has been fueled almost exclusively by service and high technology growth. A 1984 report from the State Senate's Ways and Means Committee found that 97.6 percent of job growth between 1979 and 1983 came from those two sectors, with service growth concentrated almost exclusively in the Boston area.[167] High technology growth was concentrated in three of the state's ten labor market areas, underscoring the uneven regional nature of the state's economic development.[168] The State Senate Report found that 43.9 percent of the state's population lived in areas where cumulative employment growth was only 0.7 percent between 1979 and 1983.[169] Regions with concentrations of older industries continued to decline, especially where the industrial concentrations were in nondurable manufacturing.[170]

States are not natural economic units, but geopolitical areas whose various economic activities spill across state borders and whose diverse economic sectors often have little interaction with each other. This regional variation presents challenges and opportunities to policymakers: challenges in trying to foster equitable growth in declining regions, and opportunities in that legislatures are elected on a regional basis. Helping regions is perhaps more politically acceptable than helping industries, and "industrial policies" in theory may turn out to be regional policies in practice, as different regions usually have specific industrial mixes. A region-specific policy thus may turn out to be focused on specific industries.

In a variety of areas, Massachusetts has adopted what this paper has

166. *See generally* H. RICHARDSON & J. TUREK, ECONOMIC PROSPECTS FOR THE NORTHEAST (1985).

167. MASSACHUSETTS SENATE COMMITTEE ON WAYS AND MEANS, THERE IS MORE THAN ONE MASSACHUSETTS ECONOMY; A STUDY OF MASSACHUSETTS PRIVATE SECTOR EMPLOYMENT, at vii (1984).

168. *Id.* at 2-13.

169. *Id.* at v.

170. *Id.* at 42-93.

characterized as "strategic" policies, going beyond the traditional responses to cyclical decline and instead addressing structural socioeconomic problems. One of the most notable efforts stemmed from the state's Mature Industries Commission.[171] Faced with political pressures for plant closing legislation, Governor Michael Dukakis appointed the Commission to study the problems of the state's mature industries.[172] After a year of research and debate, the Commission presented a detailed examination of the state's overall economic problems, along with a series of policy recommendations that went beyond the single issue of plant closings and the mandatory pre-closing notification that was sought by labor.[173]

Massachusetts eventually provided for voluntary prenotification on closings, but it also created a set of new programs to aid workers and firms.[174] The state backed away from the notion that some industries were "mature," noting that many of the industries that were leaving the state remained economically viable elsewhere.[175] New policies are directed at taking positive actions to help industries and workers adjust.[176] The State's Industrial Services Program is an umbrella agency that directs an early warning system to develop state economic profiles, and to monitor industries and firms in danger of shutdowns, provides financial and consultant aid to some troubled firms, and coordinates employment efforts for workers in these firms and industries, including exploration of worker buyouts and startups of worker-owned firms.[177]

Massachusetts has maintained traditional efforts like those of other states, but has also supplemented them with unique interventionist elements. Attempting to shed its derisive label of the mid-1970s, "Taxachusetts," the state has cut taxes and plans to do so again.[178] The state also pioneered the increasingly popular "tax amnesty" program to allow delinquent taxpayers to pay up with no penalties.[179] For industrial development, new research and development is being pursued in some high technology areas such as photovoltaics, marine sciences, and biotechnology through the state's "Centers of Excellence."[180]

In social welfare and training policy, Massachusetts has received favorable attention for two efforts: the Bay State Skills Corporation

171. STATE OF MASSACHUSETTS, THE GOVERNOR'S COMMISSION ON THE FUTURE OF MATURE INDUSTRIES: FINAL REPORT (1984); M. CLARKE, *supra* note 56, at 95-97.

172. STATE OF MASSACHUSETTS, *supra* note 171, at 1.

173. M. CLARKE, *supra* note 56, at 95-97.

174. STATE OF MASSACHUSETTS, *supra* note 171, at 1.

175. M. CLARKE, *supra* note 56, at 95-97.

176. *Id.*

177. *Id.*

178. Jackson, *Bringing Tax Administration Out of the Closet*, 5 J. POL'Y ANALYSIS & MGMT. 1, 139 (1985).

179. *Id.*

180. Wald, *A Hotbed of High Tech Raises Its Investment in Innovation*, N.Y. TIMES, Nov. 3, 1985, § 4, at 5, col. 1.

("BSSC"),[181] which coordinates training efforts with private employers, and the "ET Choices" (for employment and training) program to move welfare recipients into private sector jobs without the punitive aspects of traditional "workfare."[182] BSSC is a quasi-public corporation, supported in part by state funds. It conducts training for industry and employer consortiums, and targets all high-growth occupations. BSSC requires a private sector match, which may make it less effective in depressed regional economies. It has had some success in placing clients who are on public assistance or in employment programs with private sector employers, although some attribute this success to the tight labor market in many parts of the state.[183] ET Choice offers access to a variety of existing but fragmented programs, including basic skills training, job counseling, transportation, and day care, allowing welfare clients to tailor a package to their needs. The state recently has begun a program of providing loans, based on need and structured like a five-year mortgage, to firms that want to establish workplace child care centers.

Taken as a whole, these policies are more interventionist than most American policy efforts. Private sector firms are involved in a variety of linked development approaches, including making certain types of state assistance contingent on compliance with the voluntary industrial compact provisions.[184] Training programs that upgrade current workers also link efforts to employ the disadvantaged and dislocated.[185] Although many national versions of "industrial policy" have been written about and propounded in books and conferences, the emerging policy style in Massachusetts may give us a glimpse of strategic policy for industry in practice.

B. New York: An Emerging Regional Policy?

Unlike Massachusetts, New York has only recently turned to economic development issues as a central priority. The major initiative of the first years of the administration of Governor Mario Cuomo concentrated on taxation and budgetary policy.[186] Sparked by the 1984 report of the gubernatorial Council on Fiscal and Economic Priorities, which advocated business and personal income tax cuts to spur economic growth, the state has brought down the levels of personal and business taxes and has tried to reform its fiscal policy.[187]

In 1984, Governor Cuomo began to concentrate more energy on eco-

181. Wald, *Joblessness in Massachusetts Drops And, With Help, So Do Welfare Rolls*, N.Y. Times, Nov. 17, 1985, § 1, at 54, col. 4.

182. Kuttner, *supra* note 121.

183. Wald, *supra* note 181.

184. STATE OF MASSACHUSETTS, *supra* note 171, at 65-66.

185. Wald, *supra* note 181.

186. Tese, *Rebuilding New York—The Next Phase from Recovery to Resurgence* 51-52 (Report of New York State Director of Economic Development, Sept. 30, 1985).

187. *Id.*

nomic development.[188] New York economic development programs are scattered among the Commerce and Labor Departments, public authorities such as the Urban Development Corporation, lending agencies such as the Job Development Authority, and quasi-independent bodies such as the Education Department. New York's approach was first to remedy this fragmentation of initiatives, rather than launching industry-based initiatives. The governor instituted a new position, Director of Economic Development, who has oversight responsibility for the more than twenty agencies and departments involved in economic development.[189]

In September 1985, the new Director issued a "strategic plan" detailing new program ideas, along with an analysis of the state's economy.[190] The state plan did not focus on specific industries, but on such traditional factors as capital, labor, and infrastructure; it also focused on regional economic problems.[191] The report stressed the leading role of private sector firms, reiterating the state commitment to reducing taxes and improving the business climate.

In general, New York initiatives remain more traditional, falling into the category of policies that this paper has termed "adaptive," that is, focused primarily on tax and regulatory relief and other business climate measures. New York policy has continued in this vein, with a proposal for "opportunity zones" (essentially enterprise zones)[192] and a continuing emphasis on tax cuts and fiscal reform.

Although the state strategic plan identified a number of goals, including providing productivity assistance to existing firms, developing new technologies, and improving the business climate,[193] the major program effort in the first year of the new economic development policy came through regional economic development funds.[194] New York is divided into ten economic regions; the plan has made loans and grants available to each of those regions contingent on the filing of development plans by regional councils.[195] The regional proposals are to be judged on their ability to generate jobs and to leverage

188. *Id.* at 33.

189. *Id.* at 71. The first nominee would also have been the Commissioner of Commerce, joining the two positions, but that nominee withdrew his name from consideration by the legislature when certain credentials listed on his resume were alleged to be overstated and perhaps falsified. The Governor's second nominee was subsequently appointed to the directorship but was not nominated to head the Department of Commerce, resulting in a reduction in the director's power.

190. *Id.*

191. *Id.* at 33-34.

192. *Id.* at 66-67.

193. *Id.* at 51-52.

194. NEW YORK STATE OFFICE OF ECONOMIC DEVELOPMENT, GOVERNOR'S ANNOUNCEMENT ON REGIONAL ECONOMIC DEVELOPMENT PROGRAM PROJECTS (Dec. 2, 1985)(unpublished report; copies available from the New York State Office of Economic Development).

195. *Id.*

other capital sources.[196]

The regional program, which accounts for the state's varied economies, is emerging as a dominant focus in New York. The state's distressed regions have diverse industrial mixes; some are characterized by declining heavy industry (for example, Buffalo),[197] while others are characterized by a volatile mixture of rapid service industry growth and declining manufacturing (New York City).[198]

New York's political culture favors the regional approach. The New York Legislature traditionally is divided between upstate Republican Party control of the Senate and New York City and urban, Democratic Party control of the Assembly, with governors steering between the two houses. The state's organizational culture also militates against centralized policy direction. New York traditionally has myriad small organizations to administer different policies; attempts to centralize economic development policy frequently encounter obstacles.[199]

Some degree of fragmentation is inevitable in any political entity. Strong executive support is critical to the success of any policy unification effort. Without such support, new programs will fall prey to existing bureaucratic constituencies. New York's continuing reliance on traditional adaptive instruments and its reluctance to link policy to economic analysis may mean that regional concerns will continue to dominate state economic development policy. This regionalism undercuts efforts to centralize and coordinate economic development authority. The current approach, which indirectly empowers regional bodies, incurs the risk of exacerbating policy fragmentation and making it more difficult to assess particular policies and bring them into line with overall state goals.

V
Development and Strategic Planning for the Future

Mounting structural challenges to the economic well-being of states may well become one of the major issues confronting the nation in the next decade. The important adaptive policy approaches crafted by the New Deal and Great Society will not be sufficient to deal with these challenges. Fiscal constraints at the state and national levels make future large-scale expansion of government funding for social programs unlikely; states must lead the way in devising new approaches. Traditional policies must be recast to incorporate stategies that address social and economic problems on a structural level.

Some objections to strategic planning and coordinated activist policy ap-

196. *Id.*
197. Tese, *supra* note 186, at 30.
198. *Id.* at 30-31.
199. *See, e.g.*, McGahey, *An Evaluation of New York State's Employer-Specific Skill Training Grant Program* (unpublished working paper, Urban Research Center, New York University, Feb. 20, 1986).

proaches are grounded in the notion that centralized economic planning is antithetical to a healthy market economy.[200] However, every other democratic or free market nation has adopted some form of strategic policy planning.[201]

Like businesses, individuals and communities, governments should plan for the future. Occasional errors are inevitable, but more often informed, comprehensive planning efforts will yield long-term economic and social benefits.

Indeed, state governments *must* engage in strategic planning if they are to meet the challenges of the future. Certainly market forces and private sector economic activity are essential for growth, innovation, and economic efficiency. But market forces alone cannot properly allocate the costs and benefits associated with the process of "creative destruction."[202] Public sector activity is becoming increasingly intertwined with private sector forces in all modern economies, and deeper involvement is likely.[203]

To date, American policy makers have been reluctant to articulate and develop the public role in the economy, preferring to downplay or ignore the effect of public policy on the economy. This view limits the government's role to addressing the social problems generated by poor economic performance. To achieve economic prosperity and social justice, American socioeconomic policy must be grounded in a cohesive, integrated approach to government spending, taxation, and regulation.

As Robert Reich has noted, we can no longer afford the luxury of living without strategic policies.[204] The choice is between continuing with unexamined, and thus uncoordinated, policies and trying to develop and coordinate strategy based on the best information available. It might be that when it is not known what the consequences of a particular policy will be, or when no policy seems likely to be influential, the best course might be to do nothing. It is essential, however, to institute mechanisms that allow for such preliminary investigation so that policy makers can base a decision to act or to refrain from acting on accurate and complete information.

Because economic problems increasingly are intertwined with international issues, coping with the changing world economy will ultimately require new national policies rather than a patchwork of state variations. Nonetheless, states can and must use the tools available to them to meet the structural challenges outlined above. States should continue to assume their traditional role as "laboratories" in which creative new approaches may be developed and

200. Reich, *An Industrial Policy of the Right*, 73 PUB. INTEREST 3 (1983); L. THUROW, *supra* note 24.

201. Reich, *supra* note 200.

202. J. SHUMPETER, *supra* note 1.

203. R. HEILBRONER, THE NATURE AND LOGIC OF CAPITALISM (1985)(historically, capitalist economies have been adaptive and innovative; the growing involvement of public policy with the economy may simply represent the latest manifestation of this historic adaptability).

204. Reich, *supra* note 200.

tested. For example, although New Deal programs are remembered as springing forth when Franklin D. Roosevelt arrived in Washington, many of the New Deal innovations were first pioneered by state governments.[205]

The need for more creative policy may be even greater than it was in the 1930s. If necessity is indeed the mother of invention, future economic and social problems will continue to foster new policy experiments by state governments. In light of this experimentation, future historians may come to view the 1980s as the period when a new wave of innovative economic and social policy was crafted in the states. The structural challenges facing the nation's economy present an opportunity to move forward in crafting strategic policy approaches that can help us cope with our changing economy and society, and help create a more prosperous future for all citizens.

205. Skocpol, *supra* note 9.

RESPONSE

PATRICIA HANRATTY:* According to Dr. McGahey, the Industrial Services Program is probably the closest thing to industrial policy that the U.S. has right now.[1] Given the debate that has gone on about industrial policy, I prefer calling the work we do "strategic policy."[2] In fact, in Massachusetts we are pragmatists developing and implementing a strategic policy to address problems of economic change.

The Industrial Services Program is attempting to address the issue of structural economic change, as opposed to cyclical change. I would label what we do as "economic stabilization" rather than "economic development." Economic stabilization is not a term that we hear in discussions on economic policy or industrial policy, but it is a critical one today. Economic stabilization is the process through which government attempts to manage the transitions within the industries of a base economy, from one industrial base to another, or from a highly industrialized economy to a less industrialized economy. By definition, economic stabilization treats the problems of structural change in the economy. Clearly, these are major issues of the U.S. economy in the late 20th century. In Massachusetts we believe government must address these issues so that the impact on workers is minimized.

The Industrial Service Program ("ISP") and its financial arm, the Economic Stabilization Trust Fund, were created to manage the problems of economic stabilization. To accomplish this difficult task we have two types of programs: consulting services and loans to help increase the competitiveness of mature firms; and Workers Assistance Centers which provide re-employment services to laid off workers. The business and financial services are designed to help prevent plant closings and to stabilize older companies and industries wherever possible. The Worker Assistance Centers help mitigate the problems workers experience when their companies and jobs of 20-30 years suddenly disappear. Workers are retrained for new occupations and industries and/or are taught to look for and find a new job quickly. I think it is helpful to look at what we actually do in each program.

For companies, the ISP provides a combination of management and financial consulting and high-risk, low-interest loans to help small, older companies "turnaround" a difficult business situation. We have found that managers often do not know what their company's problems are or how they can be solved. They have no magical solution to tough, persistent business problems. Our cases indicate that the reasons most companies fail lie more in

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* Executive Director, Industrial Services Program, Boston, Massachusetts.

1. McGahey, *State Economic Development Policy: Strategic Approaches for the Future*, 15 N.Y.U. REV. L. & SOC. CHANGE 43 (1987).

2. *Id.*

the individual problems of the firm than in broader market difficulties. In Massachusetts, no matter how much a given industry has undergone decline in the last five, ten, or twenty years, there are still successful companies in that industry. Part of our strategy, in terms of providing management and financial consulting services, is to help businesses survive by carefully analyzing their markets and identifying market niches. We work with them to restructure debt, improve and change production processes, buy new equipment, and interact more successfully with their work forces. Restructuring debt often involves finding new lenders or investors for the company, and new managers where needed. In one in ten cases we make a low interest loan to the company to leverage or attract private dollars to the firm.

We also involve the work force in helping improve the company. When workers have some input into the company, they are often able to make substantive contributions to the management and productivity of the plant. They can frequently explain why, for example a plant is producing many defective pieces or why five percent or six percent of its production is inferior. Very often we find that the work force has very good insight into what is wrong in a company and how it might be improved. Workers often do not tell management their insights and concerns because they are not asked. In fact, workers often believe that they really do not know what the problem is because they are not in management. As we all know, there is no magic to management. Those on the plant floor see what is going on and can make valuable contributions to the company if they are consulted on a regular basis. In addition to providing business and financial services to companies, we also deal with the crises created by plant closings and major layoffs. (I will come back to the issue of crisis shortly because I think crisis can be a great motivator of change.) The ISP establishes and funds Workers Assistance Centers. These centers provide a range of employment, training, education, and counseling services to workers from specific plants. Much of what we do is providing funds for programs and coordinating existing agencies and services which should be available to the workers. By providing new funds for the establishment of multi-service centers, the ISP forces coordination among the many state and local employment and training agencies. We involve the Employment Service, the Office of Training an Employment Policy local service providers, community colleges, vocational schools, and social service agencies. We insist that people take off their institutional hats and deal with specific crises, problems, and groups of workers. All the agencies must provide services through one central, neutral site, the Worker Assistance Center. We have found that this cuts down on the loss of clients in the bureaucratic maze of agency referrals. One center is responsible for bringing all workers in from one plant, serving them and placing them in new jobs at wages comparable to their old salaries.

One of our most successful strategies for insuring responsive, worker oriented services has been work-force involvement in the centers. Unfortunately, labor involvement is often anathema to large bureaucracies. The ISP requires that workers are hired to staff the centers. This has been absolutely critical to the success of our centers.

Although I would not want to measure the success of these programs solely in terms of traditional quantitative measures, they are extremely successful in those terms. The job placement rates are between 77% to 80%. Another important measure of success is the wage retention rate; i.e. a comparison of the wage a worker made at her old job and at the new job she found through the center. The overall wage retention rate was of ISP programs is currently running at about 91%. Our original goal was 85% wage retention. Since many of our dislocated workers come from high-paying, unionized plants, wage retention is critical to maintain a good standard of living for them.

What have the results of this approach been in Massachusetts? We currently have about 13 Worker Assistance Centers around the state. They bear the name of the company from which the people are laid off. For example, we call one of these centers the Revere Sugar Worker Assistance Center and another the General Dynamics Worker Assistance Center. Those programs currently have an average placement wage that surpasses nine dollars per hour. Anyone who deals in employment training programs in the United States knows that the average employment training wages are somewhere between five dollars and fifty cents to six dollars and fifty cents per hour. Even if we consider that Massachusetts has some very good employment training programs that have high placement wages, ISP programs are still more than two dollars an hour above the average placement wages found in the traditional employment training programs.

I believe that a major reason we have had such success is because the work force is involved and will not put up with bureaucratic red tape. They do not care if we traditionally measure success by a six dollar an hour standard. They measure it by what they used to earn. Thus, a major part of our innovation in plant closing programs has been to hire workers to get around the bureaucracy and make all agencies more responsive. The work force has done this very successfully and has made enormous changes. Furthermore, I think we are going to see a ripple effect in the agencies; they will begin to change not just for these programs and projects, but in the way they look at and deal with workers in general.

Many of you may wonder why these programs exist in Massachusetts, the state with the lowest unemployment rate in the nation. Why is Massachusetts, which has consistently had one of the lowest unemployment rates in the country, paying attention to issues of transition, structural change, and economic stabilization? We are doing it, in part, because plant closings are crises with which we can and must deal. We have used these crises to mobilize state and local government. Dr. McGahey has correctly argued that social movements mobilize change. Historically, social movements often create crises which demand response, and as a result change occurs. In the case of structural displacement and dislocation, plant closings cause an economic crisis, which could lead to a social movement of the people in the plants. If there is no response to the crisis, workers will blame elected officials and may even turn them out of office. And, since the majority of workers in plant closings have belonged to unions, they are more accustomed to, and adept at having an institutional voice and at affecting policies.

I think public officials can use economic crises to our advantage. We can change the rules of the game when we have a crisis, and force bureaucratic institutions to change and respond to new needs and demands. In Massachusetts we have done just that. We have used the crises of plant closings and layoffs in older industries to create better, more responsive, worker oriented and worker run centers. These centers have successfully met the challenge of worker dislocation and have provided some of the best results in the nation.

In reflecting briefly on Dr. McGahey's paper,[3] I think there are a number of reasons why Massachusetts has accomplished so much in two years. First, there has been pressure from what was once a social movement and is now the labor movement in Massachusetts. Labor pushed for plant closing legislation, resulting in the first comprehensive mature industry legislation in the country. Second, there was strong executive leadership from the Governor, the Massachusetts Secretary of Labor, which was a newly created position, and the Secretary of Economic Affairs. Finally, some specific plant closings created crisis situations which demanded rapid response. In response to economic crises, labor groups, and executive leadership came together to create a strategic policy for economic stabilization in Massachusetts.

3. *Id.* at 71.

RESPONSE

HOWARD STANBACK:* There are a couple of points I wanted to raise about Dr. McGahey's paper.[1] I, too, was an academic for fifteen years before going into the policy side of the administration and implementation of employment and training programs for the city of Chicago. I have noticed a lot of praise that we get for coordination and strategic planning, and sometimes I sit back and say, "Wow, coordinating!" I would hate to be where we are *not* coordinating, because we work in the midst of bureaucracy and public policy and politics. There are a lot of things that drive decision-making other than rationality. So, let me begin by speaking first to this notion of strategic planning.

My title is Deputy Director for Strategic Planning. When the position was discussed and that title was developed I asked myself, what is the difference between strategic planning and any other kind of planning? As any good academic should do, I started going through the fairly voluminous recent literature on strategic planning and could not find anything consistent on how it was defined. One source said that, in fact, strategic planning is a new term for comprehensive planning. I said that did not make sense because the idea here is to try to bring some focus to the planning process. I think a lot of states and a lot of cities would claim that they in some shape or form do strategic planning even in their adaptive mode. Strategically lowering taxes to induce businesses to come to Chicago is one of our strategies. And so one of the things I think it is important to understand is that the concept of strategic planning is one of constrained resources. You cannot do everything; therefore you have to strategically select your goals and projects to achieve something tangible soon. Strategic planning tends to take one away form long-term planning and tends to focus one on some very concrete short term results. Indeed, this focus is critical for the public sector.

A part of strategic planning that also drives it, however, is the politics of the situation. Governors and mayors have to get re-elected every two or four years, depending on the state or city. Anyone who has been in the public sector knows that during the third year of a four year-term the official begins to get the type of pressure that can put her in the ground. What visible results can the official produce in the next year before the election actually takes place? Quite often, the strategy is not necessarily economic development but getting the elected official back in office. That goal drives the decision-making process in the public sector as much as any other variable. It is actually through that factor that the question of social movement comes into place.

* Deputy Director for Strategic Planning, Office of Employment and Training, Chicago, Illinois.

1. McGahey, *State Economic Development Policy: Strategic Approaches for the Future*, 15 N.Y.U. REV. L. & SOC. CHANGE 43 (1987).

I will give you some examples of constraints involved in strategic planning in order to compare the different constraints in different locations. If you know anything about the tension between the city of Chicago and the state of Illinois, you will understand why I note that James Thompson has been Governor of Illinois for ten years and that the state is not in the worst shape of any industrial state in the country. Michigan now is much further along in unemployment development than Illinois. Out of all the Great Lakes States—Ohio, Indiana and so forth—Illinois is not at the bottom of the economic barrel: the state has an 8.7% unemployment rate. Yet the Governor remains in office. There is a state Economic Development Agency responsible for the administration of a whole range of projects and programs which, if one looked at it as a list of activities, one would think there is a whole lot going on here. I think this speaks to the point that Dr. McGahey noted in his paper, that there are a lot of states with a lot of individual policies but the question is, do they make sense as a whole?[2] Do they make sense in terms of strategy?

Let me give you an example. Dr. McGahey mentioned all of the competition over the Saturn automobile plant, which eventually located in Tennessee.[3] The state of Illinois recently spent three hundred million dollars to get the Mitshubishi plant into Illinois, which amounts to roughly twenty thousand dollars per worker. That is the state's strategy: the plant is a feather in the Governor's cap. It will not do much for the unemployment rate in Illinois, but it is one strategy. Wisconsin, which I think generally has some very good strategies and policies, is spending four hundred million dollars to get an American Motors plant. In Michigan, American Motors is on the verge of bankruptcy. These kinds of strategies do not fit into the adaptive posture about which Dr. McGahey is talking.

Let me give another example. Virtually every state in the country, and particularly those which have been through some severe recent crises, has tried to give some attention to the question of welfare. The welfare system has been accused of being one of the structural constraints on a growing economy. Those in favor of welfare reform generally argue that people receiving welfare assistance will not renounce it for low-wage jobs. So far, several states have given some attention to welfare reform; some have done absolutely nothing.

Connecticut has a program similar to the Massachusetts project, called "Program for Self-Sufficiency;" the idea is that the state, combining federal JTPA[4] money and state resources, tries to develop a long-term placement program for welfare recipients. This program allows welfare payments to be used as subsidies for wages or certain commitments on the part of the business to aid the employees in developing career paths, and so forth. In other words, the program attempts to develop experience in the labor market. This is their

2. McGahey, *supra* note 1, at 43.

3. *Id.* at 44.

4. Job Training Partnership Act, Pub. L. 97-300, 96 Stat. 1322 (1982) (codified as amended at 2 U.S.C. §§ 1501-1781 (1982 & Supp. II 1984)).

welfare-to-work transition. It is voluntary. In fact, in Connecticut, it was used to replace workfare because that program was so inefficient and costly. When one has the strategic goal of jobs, and just jobs, that program and type of strategy is legitimate. All the government is concerned with, at least temporarily, is getting people off the welfare roles and into a job.

In contrast, Illinois state administrators have come up with a welfare-to-work program called "Project Chance." Project Chance is a three million dollar program; the stated goal is to get one hundred thousand welfare recipients off the roles and into the work force over the next three years. It is no accident that this plan was announced a few weeks ago and that there is a gubernatorial election in Illinois this year. Welfare-to-work is a big issue. The proposed program costs work out to about thirty dollars per placement. Anybody involved in employment and training knows that this program, if it works, would be one of the most phenonmenal *coups* in the country. The interesting thing about this program is that it is being run by the Illinois Department of Public Aid—the welfare agency—and not by the Economic Development Agency. These two agencies communicated for the first time about two hours before this program was announced and implemented; they have not contacted each other since. The administrators of this program have simply allocated three million dollars to local agencies and organizations to find welfare recipients and to find work and place them. There is very little training money in this program at all. If you get somebody out of training and into work for a single day, that counts as a placement. That person can leave after one day.

What we try to do in Chicago is require that the trainees remain on the job at least thirty days. Now that also is not much. But for the state of Illinois, one day constitutes a placement. So when Illinois gets this super credit at the federal level for having attained this high placement rate, it will be lauded as one of the best JTPA programs[5] in the country. It is actually because the programs are placing people on jobs for one day. If you focus on job placements as your goal, then your strategies allow that type of counting. On the other hand, you could focus on things such as quality of life and think about long-term impacts. In that case, you concern yourself with wage retention and the kinds of jobs into which people are being placed.

Indeed, as Dr. McGahey has said, realistic goals can be accomplished.[6] There are strategic options available if the state sets goals—and if the politics of the state allow that to happen. The one thing that we should all keep in mind is the real lesson Chicago has taught me: politics, social activism, and the movement and struggle behind strategic planning are the key. These factors set the context of what kinds of goals a state or local government will aim for and therefore what kind of strategic planning can take place.

5. *See id.*

6. McGahey, *supra* note 1, at 76.

RESPONSE

MICHAEL LUGAR:* Let me start by putting my comments in context. I am living in North Carolina and have lived there for six years. I have worked with Democratic Governor Jim Hunt on his task force for economic development. So much of my feelings about the state process of economic development is framed by the southern context. But I should say that there are more states like North Carolina than there are like Massachusetts. So I think we are getting somewhat of a skewed view listening to some of the things that Patricia Hanratty had to say.[1]

I think we have been given an ideal colloquium paper in Richard McGahey's piece[2] because it is so broad and raises a lot of interesting themes. I want to focus on three of those themes. The first we can all "the scattergun approach" or "the bandwagon approach" of state governments to economic development. The second issue I will discuss is whether it is desirable for the federal government to get out of the economic development business. The desirability of this abandonment can be taken as an article of faith, and I want to challenge that. Third is the state-level question of targeting versus what has been called here "strategic planning"[3] versus other approaches.

States and, for that matter, local governments, are moving into the economic development realm with little idea about the effectiveness of what they are doing. Programs such as industrial recruitment, incubator facilities, customized job training, and product development corporations are often put into place with little critical understanding of how they will perform. States simply do not know if those programs will achieve specified economic development goals in a reasonably cost effective way. These and other programs are typically added to the books because they have come into vogue as a strong bandwagon approach. From what Patricia Hanratty told us, there are exceptions in Massachusetts.[4] But even in Massachusetts there is no macro understanding of what the overall effects of the total state strategy are.

There are, of course, good reasons that states are in the dark about the effectiveness of their economic development programs. Program effectiveness is generally a hard thing to measure. However, states have not devoted resources to evaluating either specific programs or a given policy, which is the entire package of programs. There are political reasons for this. From a public relations perspective, governors may feel that more is better, regardless of

* Professor of Public Policy and Economics, Duke University.

1. *See Crisis and Opportunity: Economic Development for the '90s*, N.Y.U. REV. L. & SOC. CHANGE 79 (Remarks of Patricia Hanratty) (1987).

2. McGahey, *State Economic Development Policy: Strategic Approaches for the Future*, 15 N.Y.U. REV. L. & SOC. CHANGE 43 (1987).

3. *Id.*

4. *See* Hanratty, *supra* note 1, at 79.

quality. Governors seem more activist and more concerned if they are doing something, even if what they are doing does not achieve the desired effects. It would not serve their political interests to have some analyst tell the public that what they are doing is bad. So they do not hire people to do that. And even if state officials did have the will to evaluate their programs, analysts are hampered by a lack of data. They would have to do a lot of primary data research simply to find out about adjusted program size. The data that do exist are more about the availability of programs on the books than the sizes of those programs.

In Massachusetts, for example, we see a lot of programs on the books, but it is not readily apparent how big those programs are unless we spend a lot of time going to state offices and collecting data and looking at them in real programmatic terms. I have done some work on measuring total development effort on a state-by-state manner. Based on program sizes, I ran the forty-eight contiguous states by the overall level of effort and found Massachusetts to be at the low end of the scale even though some individual programs might be large, while Mississippi and other Southern states were at the high end of the scale of total program effort in industrial development. When I presented these results at a conference similar to this, a noted journalist in the audience sprang up and said that my results were wrong and that Massachusetts was doing more than any other state. I asked that journalist how he knew that. I had spent two years doing this work and collected a lot of data and analyzed it very carefully in a scholarly way. The journalist replied, "I know that because I just had lunch with Governor Dukakis and he told me." The point is that much of what we know about state policy is anecdotal and journalistic in nature. I think this is unfortunate because when one does that hard analysis, one finds that much of what is done is not effective and not cost efficient.

Industrial recruitment is repeatedly shown not to have much effect on actual business mobility. Customized job training also is a fairly costly way to prepare already employed workers for new jobs. And while many targeted loan programs are helping firms to create jobs, these jobs are at the low-wage end of the scale. When I studied the relationship between the size of targeted loan programs and wage growth, I found that it was a negative relationship. I could give other illustrations. My point simply is that in order for states to design innovative, effective and efficient programs, as Dr. McGahey urges,[5] they have to evaluate the performance of what is being used. They have to be conscious of the costs and benefits of what they do. The federal government has not always done proper evaluation of its programs, but there are some notable exceptions, especially in the welfare area. Evaluations of food stamps in Puerto Rico, the income tax program, and housing allowances, have affected the content of those policies. Similarly, thorough evaluations should be undertaken of state and local economic development programs.

5. *See* Mier & Stanback, *Economic Development for Whom? The Chicago Model*, 15 N.Y.U. REV. L. & SOC. CHANGE 11 (1987).

This brings me to my second point. Do we just buy into the extreme new federalism or do we challenge it? There are many things that states can do better or at least as well as the federal government. But there are some things the federal government still must do. There are some serious problems at the devolution of decision-making and financial responsibility from Washington to the states. First, left on their own, states will compete more than they should for a fixed number of jobs. It is easier today for North Carolina just to open its doors to new business from Michigan or Japan than it is for North Carolina to devote resources to home-grown industries. North Carolina is perceived to have a better business climate than most states. It is also in a better financial position to compete for those jobs. Should not the federal government help distribute the jobs nationally to where they are needed most?

A related point is that the cost of economic development policy could be especially high in states like Michigan and New York. State tax systems are currently less progressive than the federal system. By devolving financial responsibility from Washington to the states, we could thus move to a more regressive form of revenue. For all these reasons, I worry about the direction we are headed in. The federal government has a central role to play in economic development, by coordinating state efforts, directing states, acting as an interstate equity agent, and providing revenues to states at least as long as the federal tax system is more progressive than the state tax system.

My last point relates to the question of economic development for whom. The Chicago Plan, as I understand it, is an open-ended, fairly inclusive process, which responds, or tries to respond, to all claimants for economic development assistance.[6] Dr. McGahey includes a very wide-range of programs in his paper, presumably as a way to respond to diverse sets of claims. Perhaps economic development policies in the 90s should not be so inclusive. With limited resources, states might need to target economic development efforts of particular groups of individuals in geographic areas. It is an open question, however, how that could be done in a democratic way.

Let me conclude by quickly summarizing the three points that I have made in the hope that that will raise some further discussion. First, before states go full steam ahead, filling the void in economic development policy left by the "new federalism", they need to put a system of evaluation into place so that money is not spent foolishly. First the scattergun approach is not the right way to go. Second, as citizens and as local public officials, we need to resist the Reagan administration's efforts to get fully out of the economic development business. Third, we need to come to terms with the question of how we use policy to target those most in need without losing the broad-based support systems needed for the economic development policy to work at the state level.

6. *Id.* at 19.

DISCUSSION

PIERRE CLAVEL,* MODERATOR

AUDIENCE COMMENT: I'm Sumner Rosen, from Columbia. I have just three or four brief remarks. It is worth remembering that in the period between about 1910 and 1935, the states really were the laboratories for programs which the national government was later able to implement. We seem to be in that stage again. I hope we will not have to wait twenty-five years this time around. But that kind of optimistic perspective is worth having.

Secondly, so far, I have not heard any mention of labor unions except for Patricia Hanratty's very brief reference.[1] In the Philadelphia worker/ownership development of supermarkets,[2] the food and commercial workers played a central role in that program's success. That role is worth some attention. Also, I want to point out the work that the service employees have been doing around human capital development and health care through the collective bargaining mechanism. There are a series of models around the country that are worth studying. And it calls into question something deeper about the perception that present-day academics have about the past and the potential role of the labor movement.

This leads me to my third comment. It is worth looking at the inventory of human capital and economic development strategies that one finds in the social democratic countries, where the trade unions have been central actors, in Sweden, for example. Paying at least some attention to the value of precedents and practices in other countries can be of benefit to us. In this area Americans are enormously and tragically parochial. We pretend as though the rest of the world has nothing to teach us. In fact, the world can offer our nation a great deal of knowledge.

RICHARD MCGAHEY: I think you are right to note that I did not talk much about labor unions. Currently there are a lot of external pressures on the union movement, as well as some internal problems. A quick response to your comment would be that during the thirties, unions, unlike those of today, were very much a motivating force—particularly during the move to industrial unionization. I do not think that excludes the potential of modern unions. I think you are right to point to the potential in service unions and in growing occupations where a large number of workers or potential workers are women and minorities. I think that if unions are to work—and individual unions are working with those constituencies—your suggestions would be a way to ener-

* Department of City and Regional Planning, Cornell University.

1. *Crisis and Opportunity: Economic Development for the '90s*, 15 N.Y.U. REV. L. & SOC. CHANGE (Remarks of Patricia Hanratty) 79 (1987).

2. *See* Kreiner, *Worker Ownership as the Basis for an Integrated Proactive Development Model*, 15 N.Y.U. REV. L. & SOC. CHANGE 227 (1987).

gize them. I fear the industrial unions are shellshocked by the changes that they have experienced during the 1970s and the early 1980s. At least some leaderships simply want to go back to the 1960s. These unions would like to have the conditions under which they, or at least some of their membership, did fairly well. I do not think they can get that energy back. I would look elsewhere in new constituent groups within unions and probably in some unions being re-energized in these new sectors for a labor union role.

PATRICIA HANRATTY: One brief comment on the union aspect. Unions are absolutely critical in all of our programs. And that is not a political response; it is a policy reality. I think economic planning at the state level is incomplete without the insight, stimulation, pressure, and advocacy role that unions play. I have noted this role in detail with reference to the worker assistance programs which are actually doing employment training, placement, and things of that nature. I think that is a more traditional and more obvious role for unions. Beyond that, we have a serious concern about unions being involved in state planning.

I would go beyond unions to the work force in general. In Massachusetts, for example, as in many other states of the country, if you look at what percentage of the overall work force is unionized, it is not by any means a majority. However, if you look at the factory plants that are closing, we have found that union shops are disproportionately represented among those plants. In Massachusetts it has been an extremely important issue. What we have tried to do in terms of economic development and stabilization of unions is to set up a program called the Cooperative Regional Industrial Laboratories. Those "laboratory" programs have as their thesis that the work force is critical to economic development. They are small projects developed around specific industries. We have one in the machine trades, and we are putting up a second in the machine trades because they are regionally focused. We also have programs in the garment and needle trades, textile industries, and a number of others. Those programs attempt to force the traditional economic development agencies to incorporate the labor force into economic development strategies. They have had some success in some places. We still do not know, however, because it is a very new program, only fifteen months old. We do not know whether it will have the effect we expect, that is, a sustained involvement of the labor force generally in economic development planning.

MICHAEL LUGAR: Not only are labor unions uninvolved in the policy-making process, they are also consciously excluded from economic development policy-making. Industrial development policy has been formed as a way to keep unions out of the state. There is documentation that recruitment—which is the mainstay of economic development policy historically in North Carolina—is targeted to businesses that are not unionized. The problem that a policymaker in North Carolina has is that it is politically embarrassing for a state that is the tenth largest and growing to have to tell voters that it also has the lowest manufacturing wage rate in the country. Of course one of the main reasons for that is because it also has the lowest rate of unionization. How does the state government deal with that? Instead of eliminating right-to-work laws, or at least becoming neutral in its stance toward unions, the legislature and others in government recruit high-tech industries that come to a very small geographic area in the state and drive up the wage rate in one or two counties, so the average state wage rate rises but the disparity between those few counties and the rest of the state widens. North Carolina, like most other southern states, is becoming much more varied in its intrastate wage rate distribution even though the manufacturing wage rate is rising.

HOWARD STANBACK: In Chicago and throughout Illinois there is a large unionized population. They are, in terms of the Chicago Plan, "on the table" on all of this planning, very consciously and conspicuously. I do not want to suggest that there is a universal policy vis-a-vis organized labor. It is clear that there are points where we are in contention, particularly with craft unions, construction unions, and construction trades. Also, in terms of the ability to get minorities and women into those trades, these unions have had an extreme throat-hold for about twenty years and there has been no substantive change. But even in those situations, these unions are involved. The head of the building trades association is on several of the Mayor's major task forces. We try to utilize and strategically study the impact of unionization on the quality of life issues. We recognize the historical role that unions have played in advancing the quality of life for workers. One of the things that we have done with our JTPA funds[3] is to let all of our service providers know that getting minorities and women into these trades is our policy. We do not know how our policy is going to work.

AUDIENCE COMMENT: I'm Elizabeth Straughn, with the City University Graduate Center. Dr. McGahey mentioned the sort of paradox of having a growing GNP and a level or declining unemployment rate but a high poverty rate as well.[4] I wonder whether Massachusetts is just such an example. In spite of the low unemployment rate, there are still pockets of poverty. If you look at cities like Springfield or Holyoke, and particularly look at the Latino population there, you find median incomes of about six or seven thousand dollars a year. My second question is whether any of the panelists are familiar with the use of eminent domain as a way for cities or states to take over an enterprise.[5]

PATRICIA HANRATTY: In terms of the poverty issues, to rephrase your ques-

3. Jobs Training Partnership Act, Pub. L. 97-300, 96 Stat. 1322 (1982) (codified as amended at 29 U.S.C. §§ 1501-1781 (1982 & Supp. II 1984)).

4. McGahey, *State Economic Development Policy: Strategic Approaches for the Future*, 15 N.Y.U. REV. L. & SOC. CHANGE 43, 66 (1987).

5. *See* Hornack & Lynd, *The Steel Valley Authority*, 15 N.Y.U. REV. L. & SOC. CHANGE 113 (1987).

tion, is it simply that we traded a higher unemployment rate for a higher poverty rate? I think that if you look at the national picture there is no state in the nation where the poverty levels have not grown. Certainly, I know that they have grown somewhat in Massachusetts. As to whether they have grown in proportion to the dropping of the unemployment rate, I think the answer is no. Certainly we have pockets of poverty and I will argue that those pockets are very substantial. Further, we are seeing two types of pockets, often—unfortunately—in the same region.

For example, let us consider western Massachusetts. Springfield, Holyoke, and Chickapee are all cities in one area. Springfield is a major industrial city and, ironically, now has a fairly low unemployment rate. At the same time, it has over the past year and a half lost very significant numbers of highly skilled union jobs with high wages. The loss of these jobs is a major issue on which we are focusing right now. About two weeks ago, when there was yet another factory closing, we said, "this is it." We decided to focus on this issue. On the other hand, Springfield also has groups traditionally considered to have high levels of poverty among them: Latinos and other linguistic minorities, blacks, and a number of other groups in the community.

We use a regional approach in dealing with both the dislocation issues and the structural change issues. The poverty issues are addressed through the Employment Training program ("ET"), as well as by my agency. ET has also tried to focus on wage issues. My former boss, Evelyn Murphy, who was Secretary of Economic Affairs, got the ET program started through her agency. ET's success is exemplified by the fact that it has placed fifteen thousand people in the past three years. However, instead of looking solely at placement rates, Evelyn Murphy set the goals based on how many people we can genuinely get out of poverty. I agree. I would rather get a few placements that are out of poverty than larger numbers of placements keeping people poverty with all the accompanying problems.

Eminent domain, with which Massachusetts probably has had more experience than any other state, is a complex and controversial issue. I think that it is a very effective mobilizing tool for social progress. Eminent domain is also a very effective response to a genuine crisis because it creates an electoral and political crisis. Is it a truly effective tool for actually taking over and running the plant? We have not seen that occur yet. I do not know who has seen it occur in this country. I do not know if that would work because there are lots of problems concerning what state governments can and cannot do. It is certainly an effective mobilizing tool, but I try to stay out of the discussion of states running plants because it is not the role of state policy-makers to be its advocates.

AUDIENCE COMMENT: My name is Lester Wooten. I am project director for Energy Conservation Housing Rehabilitation for the Midwood Development Corporation in Brooklyn, New York. My question has to do with bi-state regional development planning with New York and New Jersey, and tri-state regional development planning including Connecticut as well. Specifically, I am concerned with transportation planning, or rather the lack thereof. In reviewing the current incompatible—although potentially compatible—transportation systems that link New York and New Jersey, we find a failure to do anything concerning this problem. Athough this issue has been considered by the tri-state commission as well as several other commissions which most similar bi-state situations do not have the benefit of, nothing has been done yet.

This problem has led to the underdevelopment of several areas outside of New York City, including my hometown, Newark, in two ways. First the extension of the PATH train to Newark International Airport and the Port of Newark—which includes the cities of Elizabeth in Union County and Newark—has not taken place. Second, people have tremendous problems trying to negotiate their way through the connections coming from the Jersey Shore to the Penn Railroad and transferring to the PATH train, and then transferring from the PATH to the myriad of subway lines. These train systems provide us with a good example of the lack of planning in building interstate trasportation systems: they all have different size tunnels.

My question is, with your own experiences with regional entities and regional models for planning, how would you apply them to situations like ours, which include the New York Transit Authority ("NYCTA"), the Metropolitan Transit Authority ("MTA"), and others all working in an uncoordinated manner instead of working in a more cooperative manner? Specifically, how would you do something such as a lease assessment, and generally, how would you approach the terrible transportation situation existing in this metropolitan area?

RICHARD MCGAHEY: There is no brief answer to the NYCTA and MTA problem. But you point us to a very important problem and one that I brushed by very quickly: economies spill out of regions. In our situation, New York City, northern New Jersey and reaching up into Connecticut are all part of really what I consider a single economy. Newark's and New York City's economies have more to do with each other than New York City's and Buffalo's do, but we are not inside the same political boundaries. The whole history that you point to, this complex of regional authorities, is not just a serious problem in transit planning, but also in housing. I would consider housing as being even more important in this area of regional planning. I think a lot of people have speculated about the issue of job growth in outer rings and poor populations within inner rings. Without trying to judge that complex issue, I am not sure that it is just an issue of transit.

An important study was done in Chicago. It compared blacks who lived near job locations and blacks who lived across town, and found that they both did equally badly relative to whites. The transportation situation may be telling us that there is something in transportation, but it should not be allowed to detract from housing issues and from discrimination issues. How one gets political leverage in these areas would require another panel. In making decisions on spending, how do you begin to get our elected officials to address politically some of these equity and development problems? I do not agree that it is as hopeless as you paint it. In any case, I think the challenge is how in regional entities, which are not even responsive on an electoral basis, do you begin to develop these goals? There are ways that one can think about doing that. But the issue of how one gets leverage in a complex regional economy that spills across a whole lot of political boundaries is an extremely difficult and important issue.

AUDIENCE COMMENT: My name is Peter Williams, from the Center for Law and Social Justice at Medgar Evers College. When you talk about economic development, economic development depends on human beings. The big problem in my view is that within the inner cities we have a school drop-out rate which is going to develop an underclass. In your planning, has anybody addressed the issue of not having enough skilled bodies to put in jobs ten to fifteen years from now?

RICHARD MCGAHEY: I think that is one issue that lots of people point out. I am more convinced that it is a problem of skills rather than simply a lack of education. When I say this, people hear me saying that education is not important. I am not saying that. While the public school system in our nation really is a disgrace, I think to some extent that getting control of the problem you raised is related to matching skills with jobs. It is an open question whether in fact the job creation that we have seen in a lot of cases requires more skills. It may require different skills, but the argument that minorities in particular are unemployed primarily due to their skill deficiencies is an open question. In other words, it is possible to get people all dressed up with no place to go.

Focusing on skill training and education by themselves characterized federal policy for the last thirty years. The theory is that if you give people enough skills and education, somehow they will get jobs in the labor market. I am not sure that theory is right but even if it is, we should not therefore give up on schooling. Manhattan Borough President Dinkins talked about the skills mismatch and said there was more to it than that.[6] I think that is correct. There are several relatively simple programs that one could employ within the current system. One possibility is linking youth jobs to continued school attendance in a cooperative format. Several cities have explored that possibility. For example, the Boston Compact graduates of the Boston school system are guaranteed much more than a job. The firms themselves guarantee jobs for graduates. In that way you again integrate your local development

6. David Dinkins, *Crisis and Opportunity: Economic Development for the '90s*, Keynote Address, 15 N.Y.U. REV. L. & SOC. CHANGE 3, 4 (1987).

with the building blocks needed to make it work. The problem of how you really influence the school system is probably just as complex as deciding how you can influence the transportation authorities. Again, I think that to accomplish this through political means is very difficult.