Urban Conditions—The Future of The Federal Role - A Comment

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DISCUSSANT
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National Tax Association is collaborating with JSTOR to digitize, preserve and extend access to Proceedings of the Annual Conference on Taxation Held under the Auspices of the National Tax Association-Tax Institute of America.
Richard Nathan and James Fossett propose in this paper to assess the outlook for urban policy. While they do so with the skill which characterizes the Brookings Monitoring Studies Group, their more important contribution is an overtime comparison of what they term an "index of urban distress." This brief comment will consider the implications of their quantitative findings, raise a few specific issues about the construction of the index, and conclude with a few observations about the outlook for distressed cities.

The Index

The Nathan-Fossett index is a simple combination of per capita income, the percent of pre-1940 housing, and the population growth rate. Hence, cities which are older, poorer, and growing more slowly will be ranked among the most distressed by this index. Their important finding is that there is a considerably larger disparity in the range of urban distress in 1975 than in 1960, i.e., distressed cities have tended to become relatively more distressed. They reinforce this finding by defining a "composite economic activity" index which shows that the economies of distressed cities grew most slowly over the 1963–1972 period. This important linkage between what has come to be known as "urban hardship" and the health of the local economy is too infrequently made.

There are some shortcomings in their index of urban distress. The per capita income measure is probably not a good indicator of the relative concentration of poverty, nor is it adjusted for regional cost-of-living variations. The latter adjustment, however, would only reinforce the Nathan-Fossett conclusions since the cost-of-living tends to be highest in the most distressed Northeast region. A more serious problem is with the housing age variable. It does not allow for a differentiation between housing age and quality; moreover, it implies that new housing construction is to be preferred to rehabilitation in alleviating urban distress. The distress index calculated here would not be affected by housing rehabilitation between 1960 and 1975. The third indicator, population growth rate, implies that a slower rate of growth or even population loss are undesirable. Yet less than a decade ago, the major urban issue was how to stop the population flow to the largest cities. Indeed, population decline in some distressed cities may bring about a much healthier economic and fiscal position. Moreover, slower population growth in a Metropolitan Jacksonville may mean something quite different than in a New York where it may only mean displacement to the surrounding suburbs. These few comments are meant only to suggest that the urban distress index probably requires additional dimensions.

The Outlook

Despite their finding that the most distressed urban areas have seen their position worsen over the past 15 years, Nathan and Fossett are optimistic about the outlook for cities. They reason that it is a good time for cities for a number of reasons: Federal aid to cities has been increasing and has been increasingly targeted to distressed cities; more singles, childless couples and elderly increase the preference for urban life; and higher energy and housing costs improve the city's competitive position for jobs and residents.

While these arguments are appealing, there is an equally plausible set of hypotheses which suggest a continued bleak outlook for cities, i.e., that the trends in urban distress found by Nathan and Fossett will continue. A foremost reason for this pessimism is that there are no data indicating a revival of cities; indeed, the present population growth appears to be occurring in nonmetropolitan areas. Higher energy costs may not favor cities at all, but speed a decentralization of jobs and workers to the suburbs. Likewise, changing demographics may not favor cities if preferences for more leisure time activity and warm weather continue to favor sunbelt migration.
Other factors are cause for even more pessimism. The manufacturing infrastructure in the Northeast is relatively obsolete and plant closures will likely continue, especially in the event of another recession. Structural unemployment and hard core poverty remain the major problem of central cities, and there is too little evidence of a redressing of this problem. Moreover, these social problems are less likely to be resolved in a period of Federal cutbacks in such social programs and taxpayer resistance to expanded state and local government budgets.

In sum, the Nathan-Fossett analysis shows a worsening of the relative position of distressed cities over the past 15 years, despite new social programs and increased Federal grant targeting. Without the growth in Federal, State, and Local government budget resources, with less targeting, and with fewer new programs, this trend will not likely be reversed.

INTERSTATE TAX COMPETITION*

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Governments have long attempted to influence the distribution of economic activity within their borders through the use of fiscal incentives, regulations, licensing, public facilities investments, and land use controls. But within a federal system, state and local attempts to influence the locational decisions of firms with fiscal incentives raise special questions that are less likely to arise in a unitary political system under which objectives and incentives for economic development can be applied more uniformly throughout the country.

The United States exemplifies these problems to the extreme. Only a very few states have not resorted to fiscal incentives of one kind or another to encourage economic development. A recent survey by the Academy for Contemporary Problems divided them into four broad categories:

1. Deliberate efforts to make the overall structure and rate of taxes—the “tax climate”—attractive to industry;
2. Tax incentives—specific exemptions, temporary tax abatements, or preferential assessments that lower business operating costs;
3. Industrial development bonds that allow business to take advantage of lower borrowing costs enjoyed by states and localities because of their tax-exempt status; and
4. The policy of providing new firms with certain public services, such as roadways or utility hook-ups at zero or reduced cost.

Corporate income taxes, are used in some form by nearly all states. Four states, however, have no general corporation tax based on net income (not counting Michigan, which in 1976 converted its corporate tax to a value-added tax). Among the other 45 states, 1976 tax rates ranged from less than five percent to more than 10 percent. Fifteen states had general corporation taxes that could be characterized as relatively light (effective rates of less than five percent), while 18 states had corporation taxes that could be classed as relatively heavy (effective rates of more than seven percent). Corporate income taxes are relatively heavy in most industrial states, but the relatively light list contains no states in the Northeast quadrant—only several Gulf states, and the rest scattered throughout the Midwest, the Mountain Region, and the West.

For most businesses, the property tax is the largest state and local tax. What is taxed, at what rate, and with what degree of consistency varies from state to state. In most states, the property tax is applied to business machinery, equipment, furniture, and fixtures, but in many states it is common for such property to be taxed at low rates. Some states exempt such property outright, while a small number tax it heavily. In general, most southern states can be said to

*Papers prepared at the Academy for Contemporary Problems reflect the views of the authors and not necessarily those of the Academy or its seven Member organizations.