MERCATUS CENTER
George Mason University

POLICY BRIEF
COVID-19 RESPONSE

Policies to Help Communities Recover: Economic Uncertainty

Salim Furth, Nolan Gray, and Emily Hamilton

June 24, 2020

Communities and local governments across the country face a period of extreme uncertainty. Whether or not COVID-19 is quickly contained, changes in consumer demand, supply chain structure, business practices, and regulation will reshape some of the economic life that makes cities what they are. The prospect of rapid, unplanned change is daunting, and many of the potential changes are unwelcome, but cities can make the best of this evolving situation by providing flexibility for residents and businesses to experiment, adjust, and find new patterns of specialization and trade that can be sustainable in the postcoronavirus world.[1]

In the best-case scenario, a rapidly deployed vaccine will remove the immediate public health threat of COVID-19, and preexisting patterns of economic activity will resume along familiar lines. Other, less optimistic possibilities abound, though. Two companion papers specifically address possible changes in housing needs and commuting patterns. This policy brief is more general and, unlike the two companion papers, assumes that some previously profitable economic arrangements will become, perhaps drastically, less common, and that others—some of them new and unforeseen—will gain prevalence.

To support the economy's adjustment to a new, healthy equilibrium, we suggest several policies that promote flexibility in land use and permitting. The ideas in this brief are by no means exhaustive, but the spirit should be clear: local governments should provide space and service to constructive ideas of all kinds.

There are two alternative approaches, both of which have attractive features but are not likely to be successful. One is to renounce the coronavirus and all its works, making every effort to return to the previous status quo. This tactic will become less effective the more severe the crisis becomes.

The second alternative is to plan a recovery strategy from the top, choosing an economic champion (such as a large employer or infrastructure investment) and risking dwindling city resources on its success. This approach may disproportionately benefit politically connected groups and surrenders the advantages of trial-and-error that attend our bottom-up approach.

COMMERCIAL ZONING FLEXIBILITY

Local governments slow entrepreneurship by limiting which types of businesses can exist in each "commercial zone" of a city. In Arlington, Texas, for example, some zones allow colleges but not trade schools, new car sales but not used car sales, restaurants but not catering services, and firearm sales but not farmers markets.[2] At a time of rapid change and experimentation, these land use restrictions take on heightened importance.

For example, if the risk associated with restaurant dining leads corporations to rely more on catered meals, then restaurants may decide that they can survive only by closing their dining rooms and relying on catering revenue. But doing so would violate the zoning code. Moving a restaurant to a correctly zoned location would mean breaking the lease and, in an environment of great economic uncertainty, signing a new one. Restaurateurs, their employees, their landlords, and the city's tax receipts are all better off with a surviving caterer than a folded restaurant. Of course, no one knows if this particular scenario will arise, but there is little reason to withhold the regulatory wiggle room for businesses to use land for a different purpose than what is allowed by a commercial zone.

Zoning boards of adjustment routinely provide exemptions from such restrictions,[3] and one imagines that our hypothetical restaurateurs would find a sympathetic audience. But forcing each land use adjustment through an extended and uncertain process adds cost, delay, and uncertainty. Instead, cities should amend their zoning codes to permanently add most nonpolluting business types as permitted uses in all business districts.[4]

Cities with strong housing demand can further benefit by allowing residential development in most commercial zones. Strip malls and office parks may seem like unappealing homes, but not as unappealing as old brick factories seemed in 1960. Yet many of the latter were later converted to lofts and sold to affluent urban professionals. People may not be particularly eager to live in retrofitted JCPenneys—but if that market materializes, cities with flexible zoning will benefit the most. Less speculatively, urban storefronts are often in prime locations and will be better off residentially occupied than vacantly waiting out a long economic downturn.

QUICK PERMITS FOR POP-UP BUSINESSES

Pop-up businesses often operate for just a few months, but a popular pop-up website notes that acquiring a simple business license typically takes two to four months.[5] Although that timeline may be reasonable for a predictable seasonal business, it effectively quashes the kind of economic experimentation that communities need to rapidly find their way to a new equilibrium.[6]

Although speeding up the permitting process is probably the best way to these help pop-up businesses, cities have eased the process in other ways as well. Chicago issues pop-up permits that are not tied to a single location.[7] This allows entrepreneurs to shift locations as they learn more about the shifting contours of demand, an important aspect of uncertainty. Miami Beach issues pop-up permits quickly on a "use for use" basis, so a pop-up can take over a space for the same type of use (restaurant for restaurant, retail for retail, and so on).[8]

PERMIT PROCESS REFORM

The process for pulling a permit—a business or occupational license, a certificate of occupancy, environmental review, event permits, and so on—differs by jurisdiction and permit type. However, three common problems plague permitting processes, and addressing these on a broad basis will speed economic recovery by allowing economic adjustment and experimentation to take place rapidly across all sectors.

1. Permit requirements can be vague and subjective, requiring, for example, that a building's exterior be "appropriate" to its location. Vagueness adds costly uncertainty and is an invitation to unfair favoritism on the part of officials.
2. Jurisdictions can slow-walk permits, either intentionally or by neglect. This delays job creation and investment and adds costs for the permittee.
3. When a permit is denied on questionable grounds, the appeals process often involved goes through the same officials who initially denied the permit—hardly objective arbitrators.

The Goldwater Institute promotes the Permit Freedom Act, which contains state legislative solutions to all three of these problems: clarity requirements, a "shot clock" for permit approval, and judicial review.[9] Some states and localities have addressed these problems on a case-by-case basis. Minnesota, for example, has a 60-day shot clock for all local permits.[10] And the city of Somerville, Massachusetts, made regulatory clarity a key goal in a recent zoning overhaul.[11]

AKRON TAX INCENTIVE

Policymakers intuitively grasp that low taxes are attractive to business growth. Unfortunately, this intuition is often operationalized in special deals intended to attract large businesses. Extensive scholarship has found that targeted tax incentives, unlike low tax rates for everyone, do not have the intended effects of increasing investment and job growth.[12]

At the same time, optimal taxation theory implies that tax rates on investment should be much lower than tax rates on fixed factors of production, such as land.[13] Taxing land distorts economic decisions less than taxing improvements and is more just, according to some, because the value of land depends largely on what surrounds it.[14]

Some cities—most notably in Pennsylvania—have used differential tax rates on land and improvements to encourage investment.[15] Although differential tax rates are economically sound, they have not been especially popular politically.[16]

As an alternative, Akron, Ohio, has pioneered a similar tax policy specifically tuned to the priorities of a city refusing to decline. Akron's Residential Property Tax Abatement is a 15-year tax abatement on residential investments and construction. If a resident were to, for example, invest $10,000 to replace heating and cooling systems in his or her home, the taxable assessment would not rise to reflect the new investment for a period of 15 years.

The Akron tax incentive is similar to a differential tax rate: it implicitly taxes new capital at a lower rate than old capital, which accords with optimal taxation theory. Unlike differential tax rates, however, it does not require a large land tax increase to be budget neutral.

And unlike targeted tax incentives, the Akron tax incentive does not rely on picking winners, and it promotes many small investments. The focus on rehabilitation helps the city avoid vacancies and dilapidation, which often exist alongside new, tax-funded investments.

Cities hungry for growth but wise to the failures of targeted tax investments could adapt the Akron tax incentive for commercial as well as residential investment. We recommend focusing the incentive on rehabilitation and reuse. Reusing commercial space keeps the city's infrastructure budget in check, benefits properties neighboring run-down structures, and keeps the playing field level between local businesses and newcomers.

CONCLUSION

No set of policies, no matter how wise or creative, is guaranteed to overcome a deep and painful economic crisis. In a time of great economic uncertainty, policy success cannot be judged purely by outcomes. But local governments can contribute to an environment in which the foundational economic actors (workers, companies, entrepreneurs, customers) are able to feel their way forward to new, sustainable patterns of specialization and trade.

ABOUT THE AUTHORS

Salim Furth is a senior research fellow at the Mercatus Center at George Mason University. He studies regional, urban, and macroeconomic trends and policies and has testified before the US Senate and House of Representatives. Previously, he worked at the Heritage Foundation and Amherst College. His writing has been featured in *National Affairs*, *American Affairs*, *The City*, and *Public Discourse*, and he wrote regularly for the *Wall Street Journal's Think Tank* blog. He earned his PhD in economics from the University of Rochester in 2011.

Nolan Gray is a research fellow in the Urbanity Project at the Mercatus Center at George Mason University. His research focuses on land use regulation, housing affordability, and urban design. Gray has authored numerous academic articles and policy papers. His writing has appeared in many major outlets, including *Citylab*, *The Guardian*, and *Forbes*. He is also a contributor to the *Market Urbanism* and *Strong Towns* blogs. Gray earned a master's degree in city and regional planning at Rutgers University and received bachelor's degrees in philosophy and political science from the University of Kentucky. He is originally from Lexington, Kentucky.

Emily Hamilton is a research fellow at the Mercatus Center at George Mason University. Her research focuses on urban economics and land use policy. Hamilton has authored numerous academic articles and policy papers. Her writing has appeared in *USA Today*, the *Christian Science Monitor*, *Economic Affairs*, and the *Philadelphia Inquirer*. She contributes to the blog *Market Urbanism*. She earned her PhD in economics from George Mason University in 2020.

NOTES

1. Arnold Kling has conceptualized the macroeconomy as "patterns of sustainable specialization and trade," a framework that is particularly helpful in thinking through the adjustments to a sudden, multifaceted shock. Arnold Kling, "PSST: Patterns of Sustainable Specialization and Trade," *Capitalism and Society* 6, no. 2 (2011): 1–18.
2. Don't bring a tomato to a gunfight. See City of Arlington, Texas, *Ordinances Governing Unified Development Code*, October 15, 2019.
3. Jesse Dukeminier Jr. and Clyde L. Stapleton, "The Zoning Board of Adjustment: A Case Study in Misrule," *Kentucky Law Journal* 50, no. 3 (1962): 273–350.
4. Cities can also scrap the list-based approach to commercial uses in favor of performance zoning, which puts limits on emissions, traffic, noise, and light in each district but leaves the content of the business unregulated.
5. Miriam Sanchez, "How-To Guide: License and Permits in Go—PopUp", *Go—Popup*, accessed May 25, 2020.
6. For an extended exploration of the pop-up concept, see Michael Forsyth and Lori E. Allen, "Pop-Up Program Development: Lessons Learned and Best Practices in Retail Evolution" (PowerPoint presentation, Innovate Michigan! Summit, East Lansing, MI, September 4, 2014).
7. "Chicago's Pop-Up Initiative," Chicago Business Affairs and Consumer Protection, accessed May 25, 2020, https://www.chicago.gov/city/en/depts/bacp/supp_info/chicagopopupinitiative.html.
8. Susan Askew, "Miami Beach Introduces Pop-Up Business Permits," *RE:MiamiBeach*, February 22, 2019.
9. Timothy Sandefur, *Permit Freedom* (Phoenix, AZ: Goldwater Institute, 2017).

10. Charles Marohn, “A Permit Process Should Never Take a Year. Here’s a Different Way,” *Strong Towns*, April 22, 2019.

11. Somerville by Design, *Zoning Reform Overview*, December 2013, http://www.somervillebydesign.com/wp-content/uploads/2013/12/Zoning-Reform-Overview.pdf.

12. Cailin Slattery and Owen Zidar, “Evaluating State and Local Business Tax Incentives,” *Journal of Economic Perspectives* 34, no. 2 (2020): 90–118; Joshua Drucker, Geon Kim, Rachel Weber, “Did Incentives Help Municipalities Recover from the Great Recession? Evidence from Midwestern Cities,” *Growth and Change* 50, no. 3 (2019): 894–925.

13. Ronald E. Grieson, “The Economics of Property Taxes and Land Values: The Elasticity of Supply of Structures,” *Journal of Urban Economics* 1, no. 4 (1973): 367–81.

14. Annika Neklason, “The 140-Year-Old Dream of ‘Government Without Taxation,’” *Atlantic*, April 15, 2019.

15. Joshua Vincent, “Non-Glamorous Gains,” *Strong Towns*, March 2019.

16. Mark Alan Hughes, “Why So Little Georgism in America: Using the Pennsylvania Case Files to Understand the Slow, Uneven Progress of Land Value Taxation” (working paper, Lincoln Institute of Land Policy, Cambridge, MA, July 2006).