

## **State Subsidies to Corporations Yield Little Return**

by Louis Uchitelle

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A huge, light-gray building, trimmed jauntily in blue, rises from the rolling, grassy fields on the far side of the runways at Indianapolis International Airport. From the approach road, the building seems active. But the parking lots are empty and, inside, the 12 elaborately equipped hangar bays are silent and dark. It is as if the owner of a lavishly furnished mansion had suddenly walked away, leaving everything in place.

That is what happened. United Airlines got \$320 million in taxpayer money to build what is by all accounts the most technologically advanced aircraft maintenance center in America. But six months ago, the company walked away, leaving the city and state governments out all that money, and no new tenant in sight.

The shuttered maintenance center is a stark, and unusually vivid, reminder of the risk inherent in gambling public money on corporate ventures. Yet the city and state are stepping up subsidies to other companies that offer, as United once did, to bring high-paying jobs and sophisticated operations to Indiana. Many municipal and state governments are doing the same, escalating a bidding war for a shrunken pool of jobs in America despite the worst squeeze in years on their budgets.

Their hope is that the new employees at the subsidized companies will give back their incomes to the community in tax payments and spending, more than justifying the subsidies. Critics argue that the same tax dollars produce a greater return when they are channeled into education and public transportation, for example, rather than corporate ventures. They also say that subsidies distort markets: United, for example, might not have walked away so quickly if the \$320 million had been its money, not the city's and state's.

And then there is the view, shared by Gov. Joseph E. Kernan of Indiana, that the subsidies are unnecessary, a bonus to companies that would set up shop anyway, at their own expense, without any subsidy. The national economy would benefit, if not a particular city's or state's.

That doesn't mean that Governor Kernan intends to stop offering subsidies. "I understand the argument that taking jobs away from Boston and putting them here is nationally a

zero-sum game," he said. "But Indiana, like virtually every other state, is not going to unilaterally disarm."

Far from disarming, Indiana's legislature recently revamped the corporate tax structure-- in effect offering a reduction in a company's state tax bill -- as an incentive to locate in Indiana, or to remain here. With the United fiasco in mind, the emphasis is on tax credits, the governor said, rather than upfront "bricks and mortar investments in particular projects." Indianapolis, for its part, is giving generous support to big employers like Eli Lilly, the multinational pharmaceutical company headquartered here. Lilly is getting a \$106 million package in exchange for a promise to invest \$1 billion and add 7,500 jobs by 2009.

There is no official data on how much is distributed in subsidies across the country. Alan Peters, a professor of urban planning at the University of Iowa, and one or two other academics have tried to estimate the total loss of city and state tax revenue through abatements, lower income taxes, outright payments, training grants, wage subsidies and the like. Their estimates start at \$30 billion a year and range up to \$50 billion, with Mr. Peters putting the number somewhere in the \$40 billions, based on a recent survey of tax expenditures.

"It seems like almost every state is giving away grandmother, grandfather, the family jewels, you name it, everything," Mr. Peters said. The anecdotal evidence of the escalating bidding war is greater than the statistical, he said.

The giveaways come in many forms. Iowa, for example, has just authorized \$75 million a year until 2010 to finance subsidies to corporations. The State of Washington has offered Boeing a \$3.2 billion subsidy package to locate the manufacture of its 7E7 airliner in the state. New York is creating more "Empire Zones," which are patches of land set aside in various counties where companies can locate nearly tax free. One way or another, the cities and states, in forfeiting more than \$30 billion a year in tax revenue, are channeling to the private sector enough to hire 375,000 schoolteachers at \$50,000 a year plus benefits.

Until the 1970's, the federal government financed most job-creation incentives. The emphasis was on regional development, the goal being to subsidize job creation in regions with high unemployment. But as the federal role withered and states and cities filled the void, the focus on high unemployment faded. "There is no pattern at all anymore in the distribution of subsidies," Mr. Peters said.

Here in Indiana, where the giveaways top \$150 million a year, the expectation was that United would by now employ more than 5,000 aircraft mechanics earning, on average, at least \$25 an hour. And for a while in the late 1990's, the payroll approached 2,500 mechanics.

The mechanics -- some trained locally, but the majority transfers from the airline's maintenance operations in California -- bought homes, went shopping, and paid property

and income taxes. In time, the multiplier effect of their outlays would have justified the huge public subsidy, city and state officials argue, although the benefits were somewhat offset by the increased cost of educating the mechanics' children and providing other public services for those who relocated.

"Part of an economic development strategy includes bringing skilled people here from other cities, not just creating jobs for existing residents," said Melina Kennedy, the mayor's deputy for economic development. "I say that proudly."

United Airlines conceived of the center during a period of expansion in the early 1990's, when it was buying Boeing 737's and Airbus 320's and adding flights within the United States. The goal was to keep this growing fleet in the air, generating passenger revenue, with a minimum of downtime for maintenance. The new maintenance center would help to achieve this goal by reducing the number of days required for "heavy maintenance" -- the periodic dismantling and rebuilding of an airliner required by the Federal Aviation Administration.

Ninety-three cities bid for the center, and United finally settled on Indianapolis, promising to add \$500 million of its own money to the \$320 million that the city and state raised through bond issues. United's \$500 million would go mainly into future expansion, and there was expansion. But in the end, the airline invested only \$229 million. The city, operating through the Indianapolis Airport Authority, even owns the tools arrayed in each of the 12 hangar bays, ready for the next tenant.

United plainly drove a hard bargain. But the deal was signed during the 1990-91 recession, and the hard times encouraged the state to fold some Keynesian stimulus into the agreement, said Mark S. Moore, director of public finance for the state of Indiana, and one of the negotiators. "Whether we spent the dollars or United spent the dollars, let's not forget it was a recession," he said. "We put lots of people to work building that facility for a lot of years at good wages."

For a brief period in the late 1990's, United made a spectacular success of the maintenance center. It cut by a third or more the turnaround time for heavy maintenance, getting 737's back into the air in 20 days or less. Numerous special features built into the center helped to make this possible: the mechanized, snugly fitting scaffolds, for example, which gave the mechanics easy and rapid access to every inch of an aircraft's skin; the automated parts delivery system; the sophisticated climate control that kept the temperature at a constant 75 degrees throughout the cavernous structure, allowing for the use of composites in making repairs.

Would United Airlines have built such a fine center without public subsidies or tax forgiveness? A United spokesman, Jeff Green, declined to even address the question so many years after the fact. Mr. Moore acknowledged, however, that even without a subsidy, the airline probably would have built the center somewhere in the United States.

"They had a vision for this center that would have set standards for maintenance quality and turnaround time," Mr. Moore said. "Maybe that undercuts an argument for why we should have been there to help, but I do think United's view at the time was to do things right."

So the city and state gambled, and the gamble eventually went sour. Caught up in conflicts with the unionized mechanics and pushed into bankruptcy by the abrupt cutback in airline travel after Sept. 11, United turned to cost cutting to survive. Heavy maintenance was a victim. It went increasingly to private contractors in the South, who took longer to get the airliners back into service. But the cost of using them was low enough to offset the loss in passenger revenue, airline officials said.

Mechanics in the South earning a third of the wages and benefits paid to their counterparts in Indianapolis helped to make this possible-- and last April, United closed the Indianapolis center, laying off the last few hundred mechanics still there. Penalty payments built into the subsidy agreement failed to deter the airline's executives.

Mayor Bart Peterson and Ms. Kennedy had counted on United's contract with the International Association of Machinists to deter the airline from pulling out entirely. That agreement limited outsourcing of maintenance to 20 percent of the total, and because of it, the mayor and Ms. Kennedy thought that United would keep some internal maintenance. "That's the business we were fighting to keep here in Indianapolis," she said. "When they announced that they had actually negotiated a provision to let them outsource all of it, that really surprised us."

Now the city, through its Airport Authority, is searching for a new tenant. Several other airlines have rejected the authority's overtures. Like United, they are increasingly turning to private contractors, although American Airlines agreed last month to maintain its maintenance operation in Kansas City after the city and the state of Missouri gave them new subsidies.

Fresh subsidies are not publicly on the table in Indianapolis as the city and state hunt for a new tenant. The candidates include several private contractors, although they normally rent large empty hangars, which are in abundance in the United States. The machinists are among those seeking to operate the center, and Ben Nunnally, president of Local Lodge 2294, says many of his members would accept "significantly less" in wages to go back to work as mechanics at the center.

The city and state, meanwhile, are paying \$34 million a year toward retiring the \$320 million bond issue, and the Airport Authority is paying an additional \$6 million a year to maintain the center, an outlay that United once shouldered, along with nearly \$700,000 a year for the lease.

"I will tell you," Ms. Kennedy said, "that it is painful from the city's perspective to be paying debt service on the facility" and not have the jobs. "But having said that," she

added, "it is what it is and now we are motivated, as we always have been, to fill the center."

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