A Renaissance Strategy for the Gulf Region

Testimony before the U.S. Senate Committee on Finance

By

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Hurricanes Katrina and Rita produced a national calamity of biblical proportions, or as David Brooks of the New York Times put it, of "Hobbesian" proportions. Picking up the pieces provides Congress an unprecedented opportunity to implement proven policies that have been on the drawing boards since the late 1970s, indeed they have their roots back to Abraham Lincoln and FDR.

This huge problem requires "big ideas," such as those identified with Presidents Lincoln and Roosevelt, and it is clear from his words and actions that President George W. Bush understands this and understands the magnitude of this tragedy and the scale of the opportunity.

Thinking about the agenda of an ownership and shareholder society where access to education, access to capital and access to homeownership is available to all, one is reminded of Lincoln's Homesteading Act of 1862 and FDR's FHA and GI Bill. They fit into a strategy of how to combat poverty, encourage enterprise, expand ownership opportunities and devise public-private partnership and market solutions to vexing problems of poverty and despair.

Thus, the need to rebuild the Gulf Coast provides Congress and state legislatures with the opportunity to implement big ideas that not only can rebuild in a rational and efficient manner but also could provide a model for beginning to transform the rest of the United States. **We have a golden opportunity to "green line" the Delta and Gulf Coast with government policies that facilitate and empower the private sector and private citizens, and in the process prove these policies also will work in the rest of the country.**

As we think about the government's role in assisting people to get back on their feet after Katrina and Rita, we should be thinking about how to expand private property rights and business ownership, particularly in the minority community, in order to create jobs and greater opportunity for those most severely impacted by these hurricanes. We should create rational and reasonable incentives to build a new Gulf Coast and Delta Region unencumbered by bureaucratic rules and strictures. We have an enormous opportunity to replace outmoded government programs and bureaucracies with public-private partnerships and new private institutions that are built upon the foundation of individual ownership, private property rights, personal responsibility and social justice that a stakeholder society brings.

President Bush is on the right course in calling for an opportunity zone for the entire Gulf region. His proposal was greeted recently by a Washington Post editorial labeling it a "Go Go Zone." Apparently no good deed goes unpunished.

I applaud the President's approach and agree that tax incentives should be available across the board to all legitimate businesses willing to invest the capital to rebuild.

The Post opined, inexplicably, that tax incentives offer breaks for investment but not for job creation. Did the Post editorialist ever take a look at the renaissance going on in Harlem, thanks to President Clinton's Empowerment Zone (a modified Enterprise Zone)? Have they looked at the low-tax industrial zones (maquiladoras) along the Tijuana-San Diego border? Have they noticed how low-tax, pro-business cities like Shanghai, Shenzhen, Pudong and Hong Kong are doing in China? Or the city of Dublin, Ireland, or the city of Dubai, UAE? There are many other examples and empirical evidence that show that while the president's opportunity zones need tweaking, they will work using similar incentives.

Congress recently passed legislation extending limited tax relief to the victims of hurricanes Katrina and Rita. Congress should enact follow-on legislation adding more “juice” to the president's opportunity zone idea of "green-lining" the entire Gulf Coast region as an enterprise zone with powerful tax and regulatory incentives to restore robust economic activity and jobs with homeownership and housing as key components.

In fact, we already have a bipartisan consensus on enterprise zones that formed back in 1995 around an enhanced enterprise zones bill that was supported by Spencer Abraham, J.C. Watts, Peter King, Jim Talent, Joe Lieberman, Carol Moseley Braun, John Breaux, Eleanor Holmes-Norton, among others, which was based on the old Kemp-Rangel Enterprise Zone bill of the 1980s. You also have a contemporary example from which to work in the Brownback-Fortuno-Ryan National Enterprise Zone Act of 2005.

The fundamental idea behind these bills is that private enterprise, not government, is the source of economic and social development. The failure to recognize this fact was, in my opinion, a flaw in President Clinton’s Empowerment Zones. While a sincere effort, Empowerment Zones fell far short of what was needed to spawn a rebirth of economic vitality and entrepreneurship in our distressed areas.

Empowerment Zones had only limited tax incentives, including a small increase in expensing for plant and equipment, and they were driven by a kind of Great-Society mentality with some $280 million in social services block grants. Social Services block grants are based on the failed notion that government can create jobs and prosperity. As I have said repeatedly, we must get away from this “big-brother” mentality. Government does not and cannot create wealth. The best it can do is unleash citizens’ drive and initiative to succeed in the market economy. We need to free up capital and the entrepreneurial spirit, and that is what a super-charged enterprise zone in the Gulf Coast region can do.

<u>During the next decade, Congress should allow individuals and companies in the zone or anyone outside the zone investing in it to pay federal taxes under a simplified, pro-growth tax system.</u>

Individuals living or working in the zone should be allowed to:

- pay a simple, low, single-rate tax that can be filed on a postcard;
- with no tax on capital gains;
- with no tax on income saved and invested; and
- no tax on low-income workers up to 180 percent of the poverty level.

Companies and home builders doing business in the zone should be allowed to:

- pay federal taxes under a streamlined federal tax system;
- allow full, immediate write-off of all investment expenditures and inventory purchases;
- a full deduction for all dividends paid; and
- no tax on capital gains.

I also would support another idea contained in the 1995 version of national enterprise zones act which is to allow all individuals and companies to deduct the purchase of qualified “enterprise-zone stock” (and I would suggest interest on bonds as well) from their income up to some generous limit, say $250,000 a year and a million dollars in their lifetime.

In addition to tax provisions such as these, Congress should enact broad regulatory relief to companies doing business in the hurricane enterprise zone. The President already has suspended some federal regulations for purposes of rebuilding but more is required than a piecemeal approach. What is required is temporarily holding federal environmental, labor and other economic regulations in abeyance, leaving it to state and local governments to determine which regulations are so essential to public health and safety that they should be enforced during the life of the zone.

Where education and homebuilding are concerned, wider use of education and housing vouchers are also tools that can be used. Congress should authorize education vouchers for the children living in or displaced from the hurricane region, which should be redeemable at any public or private school or go toward the education-related expenses of home-schooled children.

Congress also should take immediate action to preserve the Historically Black Colleges and Universities in the region, which include Dillard University, Xavier University of Louisiana and Southern New Orleans University. It is estimated that these schools have lost 20 percent of their student bodies. Congress should follow the suggestion of Howard University’s President, Pat Swygert and make an emergency appropriation to make up the lost tuition and fees.

Finally, it is absolutely essential that Congress use this opportunity to create the president's urban homesteading program to give displaced and otherwise low-income people an opportunity to own homes. Thanks to the "Today" show on NBC, Warner Records and my friend Tim Blixseth, $25 million has been raised for Habitat for Humanity in just two weeks. "Operation Home Delivery" will send homes to the region in several weeks down the Mississippi River to the Gulf Region.

One idea would be for Federal agencies and GSEs, such as the Federal Home Loan Bank, Fannie Mae and Freddie Mac, along with FHA, to pool resources to buy out low-income property owners, and then these newly acquired federal properties would be available for low-income people to "homestead." The money provided by the buy-out, along with perhaps, a Section 8 voucher, could be used to relocate or re-invest in property (when it makes sense to rebuild on the old site) or as a down payment on a new home. Obviously there would have to be guidelines and income limits but the homesteading idea would be an asset-based welfare and anti-poverty idea where the poor could then create the "live capital" outlined so well in Hernando de Soto's "Mystery of Capital."

Another matter where housing is concerned: Habitat for Humanity is one of the most cost effective ways to provide housing/homeownership for the most needy in our society. Because the secondary mortgage market (Fannie Mae and Freddie Mac) is prohibited from purchasing non-interest bearing mortgages, the GSEs cannot provide liquidity to Habitat for Humanity as it does for the rest of the housing market. I urge Congress to consider amending the pending GSE legislation or attaching this proposal to emergency Katrina and Rita relief legislation.

Other important ideas that should be considered are President Bush's "new markets" tax credit program, which could be targeted for homeownership, shelter, real estate and business development. New Market Tax Credits is an existing Treasury program that does just what the President is calling for and, with some minor changes, this program can be a leading catalyst for private sector reinvestment in the affected areas of the Gulf. If Congress would extend the definition of distressed areas to the parishes and counties affected by Hurricanes Katrina and Rita, raise the incentive percentage for small business equity investments and dedicate a pool of money available for the affected areas, then this program would go a long way toward increasing the private sector role in the rebuilding effort and decreasing dependency on the government. In addition, the Brownfields legislation proposed by Congressman Michael Turner of Ohio could provide a useful approach that could be tailored and adapted to the Gulf Coast to deal with environmental liability exposure, which will emerge as the rebuilding proceeds.

Many of my Republican friends are wringing their hands about the cost of undertaking these efforts. I agree that much of the cost could be paid for by reducing other nonessential discretionary federal spending - starting with repeal of the 6,000-plus pork-barrel projects contained in the recently enacted transportation bill - which has gotten completely out of control. I endorse the idea of across-the-board spending cuts on nonsecurity and nonentitlement accounts being proposed by congressional conservatives.

The Republican Study Committee should be commended for coming up with “Operation Offset,” which identifies some $50 billion in corporate pork and $300 billion in overall discretionary spending that should be delayed, if not eliminated outright.

Is $100 billion to $150 billion a lot of money? Of course it is. But as my colleague at the Free Enterprise Fund, Larry Kudlow, points out, it is an amount that easily can be shouldered by our economy which will be $13 trillion in 2006 and is projected to grow to $20 trillion during the coming decade.

As Kudlow points out, "Yes, the budget deficit will rise for a year or two, from roughly 2.5 percent of GDP to perhaps 4 percent. Big deal. The very bond markets that actually do the financing have shrugged the spending off, with Treasury issues continuing to trade around 4.25 percent. There was no 'spiking up' of long-run interest rates that might suggest a financial crisis. The stock markets, meanwhile, just registered their best third quarter in seven years."

Kudlow also points out that family net wealth — which includes the value of our nation’s businesses, bonds, stocks, and real estate — just hit an all-time high of $50 trillion. A great figure but the pie needs to be “democraticized,” not by redistributing the pieces of the pie among the poor but by giving the poor the access to capital, which will allow them to get a larger share of an even faster growing pie.

The fact is, Mr. Chairman, enterprise zones for the Gulf Coast will be relatively inexpensive and very cost effective. Every new job means a new taxpayer and a broader tax base. The 1995 nation-wide enterprise zone proposal was estimated, on the high side, to cost $2 to $3 billion over five years. The Brownback-Fortuno-Ryan National Enterprise Zones are expected to “cost” $26 billion over ten years. Clearly the cost of a Gulf Region enterprise zone would constitute a mere drop in the bucket compared to the total cost of rebuilding.

Moreover, we know the kinds of tax reforms contained in enterprise zones will work. For example, between 1977 and 1982, when the capital gains tax was reduced from 49 percent to 20 percent, the number of small company start-ups exploded by nearly 50 percent. More recently, as a result of the accelerated write-off provision (so-called “expensing”) enacted in 2003, firms' retained earnings reached an estimated four percent of potential GDP during 2004, a share not matched since the 1960s.

Even under the fairly tepid Clinton Empowerment Zones, 35 states and the District of Columbia have produced hundreds of thousands of new jobs and scores of billions of dollars of new capital investment. And, the concept has long been endorsed by the National Governors’ Association, the Conference of Black Mayors, the Council of Black State legislators and the U.S. Conference of Mayors. There is a tremendous bi-partisan coalition just waiting to be built around this concept.

Finally, in order to rise above some of the inter-agency turf competition that invariably will arise, I have urged the White House to think about appointing proven leaders of national stature like Ambassador Andrew Young, Urban League President Marc Morial, Mayor Anthony Williams and former HUD Secretary Henry Cisneros to help consolidate a bipartisan consensus. I too would be willing to contribute in anyway that might be useful and productive. As Chair of Speaker Hastert's "Saving America's Cities" Working Group, I recently have re-intensified the thinking and the work I have been doing on these issues for nearly thirty years.

In the aftermath of this national tragedy, we have an unprecedented opportunity to combat poverty and democratize capitalism so as to help people put their lives and family back together.   Combating poverty with education, home ownership, jobs and democratic capitalism is the vision for a true renaissance for the Gulf Coast and indeed the entire nation.

Thank you, Mr. Chairman.