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New Jersey Entrepreneur Zones White Paper

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<u>*Abstract*</u>

The Tax Cuts and Jobs Act passed by Congress in 2017 contains an economic development and tax incentive program called "Opportunity Zones." This program encourages investment in real estate assets but does not incentivize investments in high risk entrepreneurial businesses in poor communities. Research suggests that investments in businesses in economically challenged communities is one of the most effective ways to increase employment, reduce poverty and enhance student achievement (Gentry & Hubbard, 2000; Sachs, 2005; Caldwell, 2017). This paper describes a new approach to job creation and poverty reduction called "Entrepreneur Zones." These Zones should be located in high unemployment areas within Opportunity Zones. Businesses located in the Entrepreneur Zone with more than 50% of their employees living in the Opportunity Zone City would qualify as Entrepreneur Zone investments. The extant literature suggests that the Governor's Office and the New Jersey Legislature should pass legislation that provides tax incentives for investments into qualified Entrepreneur Zone businesses. These incentives should be significant enough to generate sufficient investment to help these businesses succeed and create local jobs. Qualified Entrepreneur Zone businesses should also receive tax credits for every new resident hired for more than 6 months. To incentivize cities to invest in these Zones, the legislation should empower the state to provide supplemental financial support to cities which have successfully utilized Entrepreneur Zone incentives to create a significant number of local jobs. These investments should reduce social program expenses in the state budget through a reduction in unemployment and poverty. This municipal support will motivate local leaders to make investing in Entrepreneur Zones a priority. This innovative program has the potential to be supported by both Democrats and Republicans because it will increase jobs and tax revenue by making investment into businesses in the poorest neighborhoods in the state attractive.

Unemployment Rate Index

Small businesses are the largest employers in New Jersey. These enterprises are the foundation of the middle class because they provide the income that residents need to survive in this expensive state. There has been very little research related to entrepreneurship and poverty in New Jersey. However, the related research from around the world suggests that increasing the number of successful entrepreneurial businesses in poor communities is one of the few sustainable ways to generate the tax revenue and employment necessary to reduce taxes and help the state through its current fiscal crisis (Hussain, Bhuiyan & Baker, 2014; Si,Yu,Wu, et.al., 2015; Caldwell, 2017). This is especially true in the poorest urban communities in the state.

Dr. Dale G. Caldwell, the creator of the "Entrepreneur Zones" concept, believes that "the best social programs create jobs." The quickest way to turn around low-income communities is to create new jobs that provide previously poor households with the income they need to pay their monthly bills on time (Arzeni, 1997; Jensen, 2017). The Unemployment Rate Index (URI) is a measure Caldwell developed to estimate the number of jobs required to make the municipal unemployment rate equivalent to the state unemployment rate. The URI is calculated by subtracting the state unemployment rate percentage as determined by the federal Bureau of Labor Statistics (4.1% in 2019) from the municipal unemployment percentage calculated by the US Census. That percentage is then multiplied by the working age municipal population. The resulting number represents the number of new jobs needed for the municipality to have the same unemployment rate as the state. The URI results are insightful because they suggest that an increase of 23,548 jobs in Newark is needed to bring the unemployment rate in line with the state while only 6,899 new jobs are needed in Jersey City to do the same thing. The URI is calculated for eight of the best known cities in New Jersey in Table 1.

Table 1 **NJ Unemployment Rate Index (URI) Table***

	Working Age Population	Unemployment Rate	Unemployment Rate Index (URI)	Jobs Needed
Asbury Park	12,327	10.8%	251.0%	825
Atlantic City	30,108	14.4%	334.0%	3,101
Camden	54,090	14.0%	325.0%	5,355
Jersey City	215,561	7.3%	169.0%	6,899
Newark	220,076	14.8%	344.0%	23,548
New Brunswick	44,728	9.5%	221.0%	2,415
Paterson	113,260	6.4%	148.0%	2,605
Trenton	66,051	13.0%	302.0%	5,878

The most effective way to create the jobs needed in the table is for the state to provide the tax incentives, regulation relief and financial support that local entrepreneurs need to help them increase profitability and employment in the local community (White, Bingham & Hill, 2003; Jensen, 2017). This suggests that the Murphy Administration and the New Jersey Legislature should work together to create these needed jobs through “Entrepreneur Zones” within the urban neighborhoods with the highest unemployment. These Zones are designated areas within a city where an increase in new successful businesses can significantly increase local employment. Businesses backed by sufficient capital in these Zones have the potential to create the jobs local residents need to climb out of poverty. To ensure that these businesses are focused on hiring local residents, businesses located in the Entrepreneur Zone with more than 50% of their employees living in the city would be the only enterprises that qualify for a tax favorable Entrepreneur Zone investment. If these incentives are attractive enough, they could result in millions of dollars of private investments in small urban businesses creating thousands of jobs for local residents in poor communities.

Opportunity Zones

The Tax Cuts and Jobs Act passed by Congress in 2017 contains a unique economic development and tax incentive program called "Opportunity Zones." This program was designed to encourage long-term private capital investment in low-income communities in the United States. The purpose of this tax incentive is to spur economic development and job creation in distressed communities by providing tax incentives to investors. However, the Opportunity Zones attract investment in real estate assets, not risky entrepreneurial businesses in poor communities. This program also has the potential to displace the poorest residents of urban neighborhoods.

Many of the "Empowerment Zones" created in the 1990s were not successful because of the weak investment incentives, program complexity and lack of focus on creating jobs and supporting entrepreneurs. Entrepreneur Zone legislation should be created to ensure that a significant amount of the money invested in Opportunity Zones is focused on increasing the number of jobs, successful enterprises and business tax revenue for municipal and county government. The establishment of Entrepreneur Zones should ensure that investments in Opportunity Zone locations are more impactful than they were in Enterprise Zones.

The legislation should provide for lower state and local business taxes and relaxed state regulations for businesses located in the Entrepreneur Zones. In addition, these businesses would receive tax credits based on the number of new employees that they hire who live in the city. Lenders and investors would also receive favorable tax treatment for loans or investments provided directly to qualified Entrepreneur Zone businesses. The state would make these financial investments attractive by providing tax credits or possibly tax deductions similar to those received for contributions to nonprofits.

The Safety Net vs. The Safety Trampoline

The federal subsidy programs that originated because of the "War on Poverty" in the 1960s have served as a "safety net," helping millions of children and adults survive the ravages of poverty. The federal free and reduced-price lunch program has done an exceptional job of providing nutritional meals to students who experience food insecurity. The federal welfare system has done a good job of providing temporary income and housing support to families facing financial insecurity. The supplemental funding to public schools in economically challenged communities has helped to improve learning for some students in poor urban and rural public school districts. However, these programs have proven to be "band-aids" that stop the "bleeding" but have not led to the elimination of the educational achievement gap between the wealthy and the poor. Poor students eat better at school, get additional academic remediation, go home to federally subsidized housing, and eat food paid for with government subsidies. However, far too often, they end up living in poverty when they are adults.

The adage, "Give a person a fish and you will feed him or her for a day, but teach the person to fish and you will feed them for a lifetime," applies to the policy changes that are needed to break the cycle of systemic poverty. Current federal academic, food, and income subsidies are the equivalent of giving a family a "fish" and expecting them to find a "river" and teach themselves how to fish. Research has indicated that children and adults who live in communities with high levels of poverty and violence frequently have weaker neural connections in their brain which negatively influences their awareness, judgment and ethical and emotional behavior

(Bronfenbrenner & Ceci, 1994; Luby, 2015). These individuals are often extremely intelligent; however, their amygdala (which controls their emotions) has been negatively impacted by trauma.

Many urban residents experiencing trauma often have difficulty focusing, communicating effectively, managing their emotions, and making good decisions about work, school, and life. They experience a continuous “Post Traumatic Stress Disorder” that negatively impacts their academic achievement as students and job readiness as adults. Caldwell calls this trauma “Urban Traumatic Stress Disorder” or “UTSD” because of the recurring impact it has on urban residents (Caldwell, 2017). Current government policy is expecting people who have neurological, emotional, financial, and educational disadvantages to compete with people who do not have these challenges by teaching themselves how to find a “river” and learn to “fish.” The result of current policies is that millions of families are trapped in generational poverty.

The problem with “safety net” public policy is that it traps people in a net from which they have tremendous difficulty climbing out of throughout their life. People who are facing significant neurological, emotional, financial, and educational challenges and are given barely enough financial, housing, and food support to survive are expected to “pull themselves up by their own bootstraps” and find success largely on their own (Swansburg, 2014). Current research suggests that it is time that the government implement a “safety trampoline” approach to reduce poverty by implementing policies and programs focused on job placement (Caldwell, 2017). A safety trampoline public policy, like the proposed Entrepreneur Zone legislation, does not catch people and keep them in educational and financial poverty for generations. This type of policy helps people who are struggling bounce up into society and become productive financially independent citizens. One essential element of the Entrepreneur Zone program proposed in this paper is that it must provide for trauma informed job training for the residents of economically challenged communities so that they can excel in the new positions created by the Zones.

The Real Poverty Rate

In 1963, Mollie Orshansky, an employee in the Office of Research and Statistics (ORS) in the Social Security Administration (SSA) developed a measure of poverty based on the Economy Food Plan of the United States Department of Agriculture (USDA). She used the results of the 1955 Household Food Consumption Survey as the foundation of her research. Her analysis did not include any other expenses besides food (Orshansky, 1963; Orshansky, 1965). In spite of her warning that this was not a comprehensive measure of poverty, her research was used by the Johnson Administration and forms the basis of today's poverty rate. This suggests that current federal poverty rates may be understated because they were not developed using some of the larger family household expenses like housing (Smeeding, Rainwater, & Burtles, 2001). This understatement of poverty may be one reason that, in some cases, the federally approved measures of poverty are greater than the federal poverty rate. For example, the free lunch rate that measures poverty in public schools is 130% of the federal poverty levels and the reduced lunch eligibility rate is 185% of federal poverty levels. The current poverty rate used by the federal government underrepresents the percentage of people who are poor because major expenses like housing, child care, transportation and healthcare are not significant components of the rate.

Creating new jobs is important. However, these jobs should pay sufficient income to enable households to pay their basic expenses. The MIT Living Wage Calculator is one of the most respected indicators used to calculate the income that households of different sizes need to make to pay their basic monthly bills in any county in the United States (Nadeau, 2015). Unlike the federal poverty rate, this measure takes into account the major household expenses like housing, transportation, child care and health care. Using the MIT Calculator and the US Census, Caldwell developed a measure of poverty called the "Living Wage Index" or "LWI." This measure is calculated by examining the latest census information on household income to determine what percentage of households earn the amount the MIT living wage calculator states is necessary to pay their bills. The LWI and the number of households earning sufficient income to pay their basic bills in eight of the best known New Jersey cities is listed in Table 2. This table also provides the percentage and number of households in "Living Wage Crisis" or "LWC" (households not earning enough to pay their bills). This data suggests that there is a major economic crisis in these eight cities. Tragically, there are 144,634 households in Newark and 97,498 households who do not earn enough money to pay their basic bills.

Table 2 **NJ Living Wage Index (LWI) Table***

	Living Wage Index (LWI) %	LWI Population	Living Wage Crisis (LWC) %	LWC Population
Asbury Park	38.54%	4,751	61.46%	7,576
Atlantic City	26.27%	3,238	73.73%	22,199
Camden	25.50%	13,793	74.50%	40,297
Jersey City	54.77%	118,063	45.23%	97,498
Newark	34.28%	75,442	65.72%	144,634
New Brunswick	36.15%	16,169	63.85%	28,559
Paterson	32.36%	36,651	67.64%	76,609
Trenton	36.84%	24,333	63.16%	41,718

Caldwell's Seton Hall doctoral dissertation suggests that the LWI can predict more than 71% of language arts and 73% of mathematics state standardized test scores (Caldwell, 2017). His research suggests that if the percentage of households who earn sufficient income to pay their basic bills is increased, student academic achievement will improve. Other studies indicate that reducing poverty in a municipality will also reduce crime, health care costs and the amount of tax dollars needed to fund social programs (Arzeni, 1997; Quigley, 2003; Morrissey, Hutchison & Winsler, 2014).

In all but one of the cities listed, the majority of households are in poverty. This explains the high levels of crime, dilapidated housing and poor student academic performance in these cities (Smith, 2005; Minsky, 2013). It is important to note that household income is the focus of this analysis. Too often the focus of poverty reduction has been on the hourly income of individuals. However, individual income is less important than household income in determining real poverty. The creation of additional jobs will reduce poverty even if there is no increase in the minimum hourly wage (Neumark & Wascher, 2007; Alvarez & Barney, 2014; Jensen, 2017). If new jobs are created, the LWI will increase leading to a reduction in poverty that will likely result in an increase in student academic achievement and drop in crime rates (Hussain, Bhuiyan & Baker, 2014; Si,Yu,Wu, et.al., 2015; Caldwell, 2017).

Bridging the Political Divide

The research suggests that the only sustainable way to increase employment opportunities and the LWI in poor urban communities is for state and local governments to create Entrepreneur Zones and provide the financial and other incentives necessary to attract sufficient investment to help businesses in these zones succeed and create local jobs. To incentivize city governments to invest in the zones, the legislation should empower the state to provide supplemental financial support to Entrepreneur Zones in urban municipalities that increase their LWI. This will motivate municipal and county leaders to make a focus on these zones a priority. The incredibly high poverty rates in urban communities are a major crisis which needs immediate attention. In this period of significant political divisions, the Entrepreneur Zone program has the potential to be supported by both Democrats and Republicans because of its economic and social benefits. This innovative program makes investing in businesses in poor urban communities attractive. The resulting investment will help to enhance the success of Entrepreneur Zone businesses which will increase employment in a way that reduces poverty and the cost of social programs.

About the Author

Dr. Dale G. Caldwell is the executive director of the Fairleigh Dickinson University Rothman Institute of Innovation and Entrepreneurship which is focused on researching, supporting and promoting entrepreneurship in New Jersey. He is the creator of the "Entrepreneur Zones" concept and the author of "Intelligent Influence: The 4 Steps of Highly Successful Individuals and Organizations" and "School To Work To Success: A Practical Guide to Finding a Rewarding Career and Enjoying Life." Dr. Caldwell's experience includes serving as the founding executive director of the Newark Alliance, deputy commissioner of the New Jersey Department of Community Affairs and a senior manager in Deloitte Consulting's health care and public sector practices. In addition, he has been the president of the New Brunswick Board of Education and the Educational Services Commission of New Jersey. In 2009, he was named the New Jersey School Board Member of the Year by the New Jersey School Board Association. Dr. Caldwell received a BA in Economics from Princeton University, an MBA in Finance from the Wharton School of the University of Pennsylvania and a doctorate in Education Administration from Seton Hall University.

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