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The 22-page report, prepared by management consulting firm A.T. Kearney, is based on surveys and interviews of 100 Internet executives and experts. It follows a similar report last year. The report reiterates the recipe for attracting and keeping Internet companies: a large pool of talent, established technology companies to support entrepreneurs, a critical mass of investment money, universities and a cadre of specialized support such as tech-savvy attorneys. This year's report adds another key ingredient: tech-friendly governments. Executives said governments could get more involved by minimizing taxes for start-ups, improving education and addressing the high cost of living.

The report outlines how Silicon Valley may be losing its edge to more attractive business spots around the world, from Germany's "Silicon Saxony" to Singapore's "Intelligent Island" and Israel's "Silicon Wadi." E-commerce revenue in the United States is expected to hit \$409 billion in two years, but growth is strong in these other hot spots. Germany is expected to hit \$62.8 billion a year in two years, and Japan will reach \$28.8 billion.

Within a few years, Europe will overtake the United States in terms of Internet users. Asia alone is expected to have 198 million Internet users, according to the study.

With the high cost of business in the Bay Area, and with e-commerce becoming less centered on the United States, governments and businesses must figure out how to maintain its leadership, the study concludes.

The report tosses out several ideas, from creating a regional government for the area, to devising policies that turn Silicon Valley into a giant business incubator that nurtures young companies and then sends them away as they become stable. Another plan is to stop encouraging new start-ups to move to the area, focusing instead on the companies that are already here.

The incubator idea seemed too limited a vision for Silicon Valley, said Daphne Carmeli, president and chief executive of an e-commerce start-up called Metreo Inc. The business-building infrastructure of the valley is too valuable, she argued.

"Sand Hill Road cannot be franchised like Starbucks," Carmeli said.

As for their role in helping Silicon Valley keep its edge, local governments can't solve housing and transportation problems without enough money. Property taxes and sales taxes are the

main source of revenue for local governments. For Rosemary Stasek, Mountain View's mayor and herself a Web developer, both sources of cash are shrinking. Mountain View's annual sales tax revenues fell by \$5 million since its peak in 1996-97, in part because of Internet purchases that aren't taxed. Stasek said she could trace individual sales transactions in which Mountain View lost \$500,000 in taxes.

Meanwhile, she said, cities are stymied by the loss of property tax revenue under both Proposition 13 and a later shift of property tax money to schools. Approved in June 1978, Proposition 13 limits property taxes in California. It cuts the maximum property tax rate to 1 percent and froze value assessments at 1975 levels, until the property changes hands. Local municipalities and schools, among others, were hit. In 1992-93, the state government took another bite out of the local municipalities' pool of property tax revenue, shifting much of it to schools. Since then, the city of Mountain View, for instance, has lost \$22 million.

That's a significant chunk of change for a city whose annual budget is only about \$67 million, Stasek said.

Economists argue that this tax structure indirectly contributes to the housing shortage in the Bay Area because it creates a financial incentive for local governments to build commercial projects -- such as malls -- instead of housing. Governments can earn more from the sales taxes generated at stores, for instance, than on residential property taxes. They need the money to pay for things such as parks and sewers and streets.

From time to time discussion arises about repealing or tweaking how money is allocated under Proposition 13. With the region facing a housing crisis, talk now has risen above the murmur level, says Ruben Barrales, Joint Venture's president and chief executive.

``It's definitely audible at the state level," he said. ``It requires a push from private industry."

Contact Jennifer Bjorhus at [bjorhus@sjmercury.com](mailto:bjorhus@sjmercury.com) or (408) 920-5660.



Government urged to help tech (10/12/2000)



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