

# **THE PUBLIC FINANCES OF A WELL RUN CITY**

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# **THE PUBLIC FINANCES OF A WELL RUN CITY**

*LEARNING FROM DETROIT*

**STEP 1: LET'S NOT REPEAT (DETROIT'S) HISTORY**

*HOW TO HAVE A FISCAL CRISIS*

**STEP 2: THE RULES FOR SOUND CITY FISCAL POLICIES**

*WHAT TO DO, AND HOW TO DO IT*

**STEP 3: GETTING THE INCENTIVES RIGHT**

*EMPOWER THOSE WITH A STAKE IN THE GAME*

# STEP 1: LET'S NOT REPEAT (DETROIT'S) HISTORY

## *HOW TO HAVE A FISCAL CRISIS*

**WEAK DEMOGRAPHICS + WEAK ECONOMY + WEAK POLICIES**

38% Poor

30% Job Loss 2000-12

Labor Policies

12% Elderly

23 to 36% UE in 2010

Unfunded Pension

25% Fall in Population 2000-10

Rolled-over Debt

Decaying Infrastructure



**FISCAL CRISIS**

**16% Fall in Property Since 2010**

## **STEP 2: THE RULES FOR SOUND CITY FISCAL POLICIES**

### ***DECISION NO. 1: What Should City Governments Do?***

#### ***RESIDENTIAL SERVICES***

Education: Pre-K; K-12; Community College

Police and Fire Protection; Courts and Prisons

Sanitation Services; Water and Sewer;

Open Space, Parks and Recreation, Libraries

Neighborhood Roads

## *BUSINESS SERVICES*

Police and Fire Protection; Courts and Prisons

Sanitation Services; Water and Sewer

Commuter Roads; Public Transit; Parking Garages

*BUT WHAT ABOUT INCOME REDISTRIBUTION?*

Services for Lower Income Households

*(Providers but not Financiers)*

A 3% Increase in Rate of Poverty → 25% Fall in Home Values

## *How Should Cities Pay for What They Do?*

*Residential and Business “Excludable” Services:  
Education, Sanitation, Water, Sewer, Libraries*

Average Variable Costs = User Fees

Fixed Costs = Debt plus Taxation

*Residential and Business “Non-Excludable” Services:  
Protection, Roadways, Open Space, Courts/Prisons*

Average Variable Costs = Taxation

Fixed Costs = Debt plus Taxation

*BUT WHAT TAXES?*

**Rule No. 1:**

*Tax it Where it Lives, Not Where it Works!*

Residential Income Taxes

Land Value Taxation

“Neighborhood” Property Taxation

**Rule No. 2:**

*Resident Taxes for Resident Services and  
Business Taxes for Business Services*

Land Value Taxation

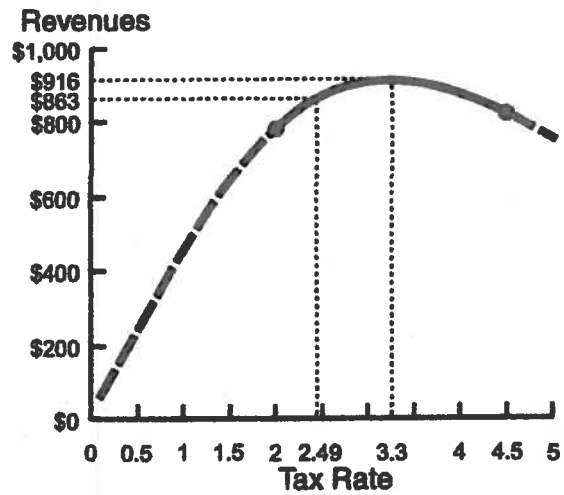
“Business Zone” Property Taxation

## Rule No. 3:

*PLEASE, Don't Go to the Top of the Revenue ("Laffer") Curve*

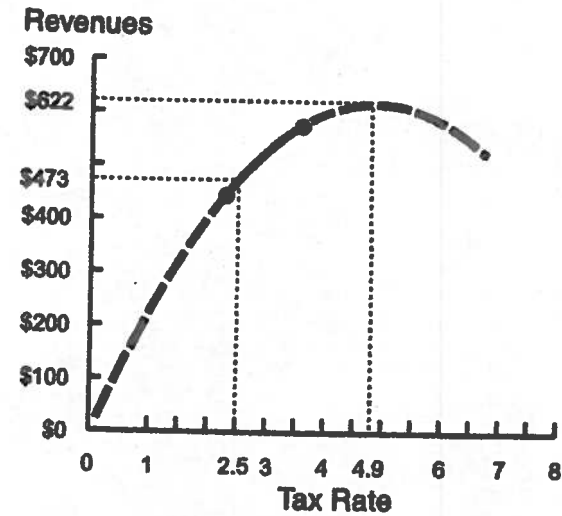
### New York

#### Property Tax



### Philadelphia

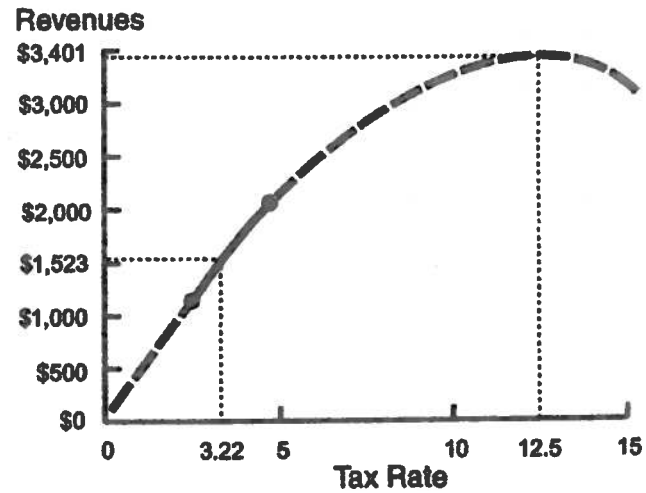
#### Property Tax





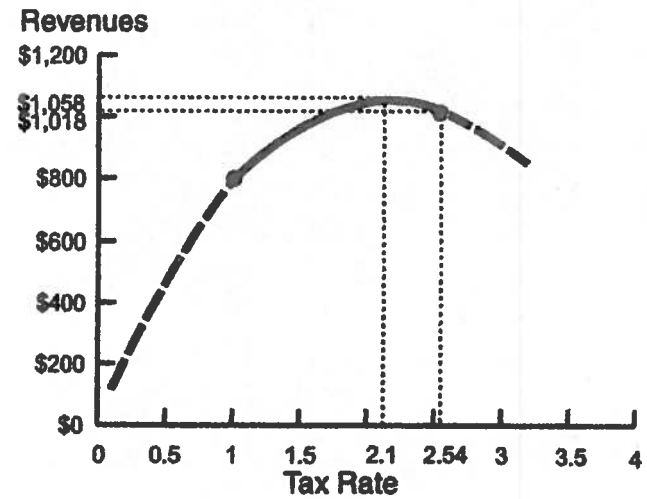
## THE "GOOD"

### Minneapolis Property Tax



## THE "UGLY"

### Houston Property Tax



SOURCE: Andrew Haughwout, Robert Inman, Steven Craig, Thomas Luce, "Local Revenue Hills: Evidence From Four US Cities," *Review of Economics and Statistics*, May, 2004.

## **Rule No. 4:**

*Financing Services for Lower Income Households*

REGION? STATE? NATIONAL?

*Does Regional Financing Help the City's Economy?*

County Sharing of Welfare Costs adds 13% to Home Values

(And Suburban Home Values May Rise Too!)

SOURCE: Andrew Haughwout and Robert Inman, "Should Suburbs Help Their Central City?"  
*Brookings-Wharton Papers on Urban Affairs, 2002*, Tables 5 and 6.

## STEP 3: GETTING THE INCENTIVES RIGHT

☞ *Strong Mayor Form of Governance, **Not** a District Council*

Agenda Powers; Veto With 2/3's to Override; City-Wide Elections

☞ *Contracting Out for Service Provision Allowed*

Competitive Alternatives; Contract on Price; Monitor Quality

☞ *“Power to the People”*

*Neighborhood Governance using NID's:*

*Providing:*

Education, Police, Sanitation, Libraries, Recreation, Open Space

*Financed by:*

User Fees & Neighborhood Property Taxation for *Efficiency*

Across Neighborhood Equalization Grants for *Fairness*

*Business Zone Governance Using **BID**'s:*

*Providing:*

Police, Sanitation, Open Space

*Financed by:*

User Fees & Business Zone Land Taxation

## AND LAST BUT NOT LEAST:

☞ *It's Always Nice to Have a "Gorilla in the Closet"*

Gorilla No. 1: State Balanced Budget Requirements

- *Ex Post* Balance, not *Ex Ante*
- *No Overrides*
- *Independent Enforcer with Significant Penalties*

## Gorilla No. 2: Fiscal Control Board

- Politically Independent
- Credible Evaluation by Competent and Independent Staff
- Credible Enforcement for Violations of Budget Balance

*Deny State Aid (PICA); Deny Bond Guarantees (MAC)*

# CONCLUSIONS

WELL DESIGNED FISCAL INSTITUTIONS



WELL CHOSEN FISCAL POLICIES



STRONG LOCAL ECONOMY



HIGHER INCOMES & HOME VALUES, ECONOMIC OPPORTUNITY