

# Bloomberg

## Government, Not Globalization, Destroyed Detroit

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Free markets and limited government are to blame for the largest municipal bankruptcy in U.S. history. That is the new meme to explain Detroit's plight. Former Michigan Governor Jennifer Granholm blames "free trade" for the decline of Detroit's auto industry and thus the city itself.

New York Times columnist Paul Krugman suggests that "for the most part the city was just an innocent victim of market forces."

MSNBC's Melissa Harris-Perry claims that "this is what it looks like when government is small enough to drown in your bathtub," referring to conservative Grover Norquist's famous nostrum about the ideal political system.

Another MSNBC contributor, Michael Eric Dyson, suggests that "racial animus" was the real culprit.

Detroit has indeed had its share of racial problems. A long history of discrimination exploded in riots in 1967, followed by white flight to the suburbs. And as an almost-single-industry town, Detroit was hit hard by the decline of General Motors Co. (GM), Ford Motor Co. and Chrysler Group LLC.

Yet other cities, such as Pittsburgh and Cleveland, that have struggled with the same challenges have managed to bounce back or at least stay afloat. And auto manufacturing continues to thrive in states such as Alabama and Tennessee.

As for "small government" being to blame, one has to go back 52 years to find Republicans in control of Detroit's government. Even then, one would not mistake Louis Miriani, the city's last Republican mayor, for Norquist.

No, one has to look elsewhere for the reasons Detroit hasn't been able to recover from its troubles.

### *Unfunded Obligations*

The most obvious candidate is the city's vast unfunded pension programs, which have been running deficits for years. Fully 99.6 percent of the city's retiree health-care liabilities are unfunded, and the program generally pays 80 percent to 100 percent of retirees' medical costs. From 2007 to 2012, the city's two biggest pension programs paid out \$3.3 billion more in benefits than they took in through contributions or investment income. Unfunded obligations account for \$9.2 billion of Detroit's \$18 billion debt: \$3.5

billion comes from the pension part and \$5.7 billion comes from the retiree health-care liability.

The individual pensions for public employees are fairly modest, averaging some \$18,000 a year, but they are spread over a huge past and present workforce. Detroit's political establishment has long been based on patronage. Although the public workforce has shrunk in recent years, almost 1 in 15 residents still works for the city. Salaries and benefits for current employees consume 36 percent of the city's revenue. Legacy obligations, which include pension contributions and benefit payments, take an additional 39 percent of revenue. That leaves little to invest in the failing infrastructure.

Pensions are hardly Detroit's only hurdle. The city throws plenty of money at its schools, which are beholden to the powerful Detroit Federation of Teachers, spending more than \$14,000 a student annually. Yet little value is received in return: In 2009, Detroit public-school students turned in the lowest scores ever recorded in the national math-proficiency test. More than a third of students fail to graduate.

In many ways, Detroit is a model of tax-and-spend liberalism. The city's per-capita tax burden is the highest in Michigan. Detroit has the country's highest property taxes on homes, the top commercial property tax and the second-highest industrial property tax.

The city's income tax -- 2.4 percent for residents, 1.2 percent for nonresidents and 2 percent for businesses -- is the highest in Michigan. The income tax burden on residents is significantly higher than that for those who live in the surrounding area, which helps drive more affluent and successful residents out of the city. And Detroit is the only city in Michigan that has an excise tax on utility users.

### *Crushing Business*

Besides the anti-business taxes, there are the anti-business regulations. The city imposes a "living wage" of \$11.03 an hour (\$13.78 an hour if other benefits aren't provided) for public employees, as well as on businesses that contract with the city. This year, Detroit started a campaign against businesses that don't meet the city's voluminous licensing requirements, promising to shut some 1,500 "illegal" ventures such as tire shops and secondhand appliance stores operating out of abandoned warehouses. This sector makes up almost a 10th of businesses operating in the city and serves almost 70 percent of residents. The official policy is to crush these operations.

A few years ago, the nonpartisan Bay Area Center for Voting Research rated Detroit as the most liberal city in America. The city's own choices, not free markets and limited government, are really responsible for Detroit's failure.