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RESEARCH SUMMARY

CAN POWER BE RESTORED IN THE ELECTRIC CITY?
A Case Study of Scranton, Pennsylvania

Once a robust producer of coal, iron, and steel, Scranton, Pennsylvania, is perilously close to financial insolvency. This situation stems from decades of increased government spending in the face of a declining population, a shrinking economy, and an eroding tax base.

A new study for the Mercatus Center at George Mason University thoroughly reviews the relevant economic indicators and fiscal policies to show how the city fell so far. The success of a service-oriented economy relies on (1) a business environment that encourages entrepreneurship, (2) the efficient provision of government services, and (3) a pleasant climate rather than natural resources. Because Scranton cannot control the weather, it needs to work with the state government to create a business climate that fosters economic growth and is able to withstand industry-specific shocks such as those that crippled the city's coal and steel industries.

To read the study in its entirety and learn more about its authors, Mercatus Senior Research Fellow and Director of the State and Local Policy Project Eileen Norcross and Mercatus Research Fellow Adam A. Millsap, see "Can Power Be Restored in the Electric City? A Case Study of Scranton, Pennsylvania."

ECONOMIC HISTORY AND FISCAL FACTORS LEADING TO DISTRESS

During the late 19th century, Scranton, Pennsylvania, was a bustling industrial city. The manufacturing workforce buoyed an economy that relied on coal, iron and steel, and railroads. The confluence of the Great Depression, the rise of natural gas and oil as energy substitutes for coal, and the rise of truck transportation to compete with the railroad led to not only a major shift from a manufacturing to a service economy, but also a huge population exodus. From its peak of more than 143,000 people in 1930, Scranton's population fell by nearly half to an estimated 75,281 in 2014. Policymakers have failed to adjust to a changing population and economy.

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Failure to control employee costs.
As goes a city's population, so go its tax base and municipal coffers. But Scranton has not made the operational adjustments necessary to offset the revenue lost by such a population decline. To the contrary, state and local government steadily increased in size and cost from 1969 to 1980, spreading more costs over fewer people. The growing dichotomy between the cost of Scranton's services and its economic base is rooted in an inability to control employee costs that is largely owing to collective bargaining, inadequate pension funding, reliance on debt to cover services and projects, and a complex local and state aid structure.

Fiscal distress and failed recovery plans.
In 1992, the Commonwealth of Pennsylvania classified Scranton as a fiscally distressed municipality. Yet five recovery plans over nearly 25 years have failed to fix these problems:

- The plans included mixtures of borrowing, nonprofit contributions, wage freezes, employee cuts, healthcare caps, skipped pension contributions and escrow funds, and privatization efforts.

- None of the plans worked as a wholesale, long-term solution. In fact, many of the state's own policies regarding collective bargaining, pensions, and taxation exacerbated the city's poor fiscal management and ongoing structural deficits. For instance, the state sets the parameters for municipalities to negotiate pensions and subsidizes these plans; however, pensions are negotiated at the local level. This means promises are made at the local level but subsidized by state taxpayers.

REGIONAL CONTEXT

The impact of any fiscal reform depends on how Scranton stacks up against its neighbors. This study compares Scranton to other Pennsylvania cities in population, wages, home prices, and education levels—all indicators of the potential for economic diversity and growth:

- The relative isolation of Scranton puts it at a geographic disadvantage to several other cities, which are able to leverage the products, services and jobs of larger, closer cities like New York City and Philadelphia.

- Scranton also ranks lower among comparable cities in income, median home prices, and education levels. All these factors make Scranton less likely to attract young professionals who can launch and grow a new, diverse economy.

RECOMMENDATIONS

Serious reform must take place at both local and state levels to bring the cost of services in line with the city's ability to pay. Reforms should address the following:

- *Employee compensation*. Limit collective bargaining, divest assets, and introduce competition for government goods and services through privatization and subcontracting.

- *Taxes*. Eliminate or drastically reduce the business privilege tax, mercantile business tax, and Local Services Tax; revoke the tax-exempt status of organizations that do not meet the definition of “purely public charities” to broaden the property tax base; and potentially lower future property taxes.

- *Pensions*. Cap current pensions, close plans, and give government employees the option to enter a new defined contribution system rather than the current defined benefit system.