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TIEBOUT OR SAMUELSON: THE 21ST CENTURY DESERVES MORE

EDWARD J. HUCK*

For more than 35 years, the issue of municipal consolidation has brought attention to an article, *A Pure Theory of Local Expenditures*, by Charles Tiebout.¹ Tiebout's article, a rebuttal of an article authored by economist Paul Samuelson, has defined the boundaries of modern urban policy debate. Advocates of both Tiebout and Samuelson contend that the authors articulate polar opposite opinions in the still-hot debate on whether it is better government to have a myriad of small municipalities or fewer large units of government. Samuelson emphasizes social and economic justice, and Tiebout advocates economic efficiency.

I contend they are not mutually exclusive in terms of an outcome. That is, it is not necessary to consolidate in order to reach economic and social justice, but consolidation may be the final outcome if Tiebout's publication is taken as gospel.

Here is the story. In 1956, when centralizing government was a pretty intellectually appealing answer to the problems of social economic efficiency, Tiebout voiced a compelling argument against consolidation. He advocated that providing a range of local municipal choices was imperative because "people vote with their feet." That is, people will simply move to a community that offers a level of services that suits them.² In Tiebout's model, each citizen chooses the community that best satisfies his or her own particular demands. Competition, thereby, provides that all citizens in each community agree on their service levels. Today, Tiebout's followers believe that local competition is the perfect solution.

Tiebout strongly refuted Paul Samuelson's 1954 article, *The Pure Theory of Public Expenditures*.³ Samuelson had analyzed the "free rider problem," the concern that some folks would try to reduce their own tax burden while enjoying the benefits of services supplied by another taxpayer. This free

* Executive Director, Wisconsin Alliance of Cities. Presentation at the Wisconsin Tax Policy Colloquium, Marquette University Law School, April 15–16, 2004.

1. Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956).

2. *Id.*

3. Paul Samuelson, *The Pure Theory of Public Expenditures*, 36 REV. ECON. & STAT. 350 (1954).

ridership creates a range of tax and service disparities for municipalities. In Samuelson's model, because markets do not always provide public goods efficiently, some form of governmental intervention is needed. Today, many of Samuelson's followers advocate the merger of multiple municipalities by state or federal mandate.

The polarism created by Samuelson and Tiebout reappears today whenever there is talk of municipal government mergers, annexation, or regionalism. The questions of economic and social justice, or for that matter, economies of scale and diseconomies of scale, almost never seem to seep into the discussion together. We continue to create neat little boxes of debate; big is bad and small is good or vice-versa. Rarely are these points of view exclusively right. *How about the possibility that both Tiebout and Samuelson are right, at least partially?* What if we reframe the urban policy debate along multiple dimensions?

If we agree that "Tiebout's Hypothesis," which assumes that citizens can "vote with their feet," is correct only in that persons with certain incomes have that ability, then we can move forward and deal with exclusionary zoning and racism. In 1957, neither was much considered. Nor were there many differences in corporate culture, ownership, or behavior. Today, "[c]ompanies increasingly go, and are started, where talented and creative people are."⁴ Not so in 1957. Let us not use Tiebout to continue racial segregation along with wealth and poverty segregation in 2004. The point often made is that any government organization that prevents the mobilization of a people because of race is wrong.⁵ But does this mean regional government? Does this mean municipal mergers are the only way to achieve social and economic justice?

We should also recognize that Tiebout was right about providing government services that may become less useful to others or have little utility for others. People who have the income to move will move when they feel the services and the environment provided by their city no longer justify the taxes they pay. We cannot rope them in. We must find ways to focus on efficiency and quality of life. Building walls to keep people in is not any more right than keeping them out. So now what?

4. RICHARD FLORIDA, *THE RISE OF THE CREATIVE CLASS* 283 (2002).

5. REFLECTIONS ON REGIONALISM (Bruce Katz ed. 2000); BRUCE KATZ & MARGERY AUSTIN TURNER, *WHO SHOULD RUN THE HOUSING VOUCHER PROGRAM? A REFORM PROPOSAL* (2000), at <http://www.brook.edu/es/urban/vouchers/report.pdf>.

I. MAYOR HENRY MAIER, BRUCE KATZ, MYRON ORFIELD, DAVID RUSK,
AND ME

I started working for city governments in 1984. The Honorable Henry Maier was Mayor of the great City of Milwaukee. You could count on the Mayor for two quotes: "Those bastards at the *Milwaukee Journal*" and "Those goddamn suburbs!" The Mayor, as well as every mayor today, knows that a full-service city must prepare to serve both daytime and nighttime populations. The infrastructure and services provided 24-7 to families, commerce, and its workforce, health care facilities, universities, and many other institutions of learning and government serve many people beyond the residents of the city. Mayor Maier was constantly aware that people of wealth could live near his great city and never pay for all the benefits it provided. Today, those first-ring suburbs are Milwaukee's allies against a new ring of suburban growth. Eventually, this new ring will join an unenviable club. The fact remains that when concentration of poverty and wealth are in close proximity and in different political jurisdictions, there are going to be problems that cannot be solved within the borders of any single jurisdiction.

Before someone accuses me of being an apostle of Bruce Katz, Myron Orfield, and David Rusk, let me declare that I am an apostle of Bruce Katz, Myron Orfield, and David Rusk.⁶ I also believe in regional solutions. These men have brought new and exciting ideas on revenue sharing, housing policies, race, and income policies. Like a breath of fresh air, they filled me with ideas and energy to find a new way for Wisconsin.

For almost 20 years, I have worked for more than two dozen mayors who govern cities that range from 8500 to 575,000 in population. They all know the importance of serving the public, which is no small task. Their work, which used to receive accolades and honor, is now chastised by state and federal politicians trying to make points with a cynical public, both on the left and right of the political spectrum. City leaders' goals are related to building their cities through economic development, housing development, transportation systems, and a quality of life that entices young people, regardless of race or religious orientation.

What these leaders need are the tools to govern better. Those tools can take shape by looking at a natural economic area (Metropolitan Statistical Area) and creating a regional focus for land use, housing, transportation, economic vitality, and revenue sharing.

6. See *supra* note 5. See also MYRON ORFIELD, *AMERICAN METROPOLITICS: THE NEW SUBURBAN REALITY* (2002); MYRON ORFIELD, *METROPOLITICS: A REGIONAL AGENDA FOR COMMUNITY AND STABILITY* (1997); DAVID RUSK, *INSIDE GAME/OUTSIDE GAME* (1999); DAVID RUSK, *CITIES WITHOUT SUBURBS* (2d ed. 1995).

II. REVENUE SHARING CAN REDUCE THE NEED TO CONSOLIDATE

In Wisconsin, we have a system of intergovernmental transfer from state revenues called "state shared revenues." It is a program with the goal to neutralize tax base and tax rate differences among local governments. Through the shared revenue program, Wisconsin distributes state tax revenues to municipal and county governments for use at their discretion. The program is a fundamental element of Wisconsin's local finance structure and the state's overall program of property tax relief.⁷ Wisconsin's practice of sharing state taxes with local governments dates back to 1911, when a share of the new state income tax was earmarked for local governments to compensate them for property tax exemptions for intangible property and household furnishings.⁸ The shared revenue program is successful, but it is constantly under siege. The state budget allocates each year more than \$900 million of general-purpose revenues into the program. This irritates some conservative legislators, who believe in the Tiebout theories, even if they are not aware of the genesis of their thoughts. The truth is, however, the program does a decent job of making sure that every municipality in the state can compete for jobs and people. Most of the revenue is distributed through an entitlement that uses two factors: (1) per capita property wealth and (2) net local revenue effort. The lower a local government's per capita property wealth and the higher its net revenue effort, the greater the local government's revenue entitlement.⁹

Why is such a wonderful program not duplicated more often? Because Tiebout's hypothesis is often used to confuse the public and accuse local governments of spending other peoples' money. Of course, no one questions the practice in the NFL where teams share revenue to ensure each team can compete. That is a good thing. My friend and colleague Dan Thompson, Director of the League of Wisconsin Municipalities, points out that revenue sharing occurs within every city today between rich and poor. It just goes unnoticed. This is why the consolidation of many cities into one or the creation of a regional government is appealing to so many politicians.

The criticisms of shared revenues in Wisconsin are twofold: first, it is too closely tied to spending at the local level, and second, there is no connection between revenues received from the state and revenues raised locally. The criticisms are more political than policy, but they are threatening to the program. The spending issue can be addressed by going to a foundation plan

7. Information Paper, *Shared Revenue Program*, WIS. LEGIS. FISCAL BUREAU.

8. *Id.*

9. *Id.*

and by defining “need.”¹⁰ A foundation plan would require a mill rate effort before state aid would be given. Need can be defined by measuring relative income, poverty, and property values within a defined region. The logistics of regional revenue sharing are more difficult.

III. REGIONAL GOVERNMENT WOULD REQUIRE A CONSTITUTIONAL CHANGE

In Wisconsin, cities and villages have constitutional “home rule” powers. This means that unless the state legislature expressly restricts cities and villages from an action, the local government can go forward. I mention this because county government does not have constitutional legal standing. That is, city and village governments are legally stronger than county government. To further complicate legal matters in Wisconsin, there is case law that says that state government cannot force one level of government to levy a tax and give it involuntarily to another level of government.¹¹ This makes regional revenue sharing, as most would conceive it, impossible under current law.

Functionally what this means is that, in order to create tax-base sharing, the state would need to create “regional government.” There would have to be a constitutional change that recognizes regional government and places it within the context of Wisconsin law.

IV. CONSTITUTIONAL CONVENTION

In 1846, the Wisconsin Territory held its first constitutional convention. Article XVIII, section 2, stated:

Every tenth year after this constitution shall have taken effect it shall be the duty of the legislature to submit to the people at the next annual election the question whether they are in favor of calling a convention to revise the constitution or not; and a majority of the qualified electors voting thereon shall have voted in favor of a convention, the legislature shall at its next session provide by law for holding a convention, to be holden [sic] within six months thereafter; and such convention shall consist of a number of members not less than that of the house of representatives, nor more than that of both houses of the legislature.¹²

10. MYRON ORFIELD & THOMAS LUCE, *WISCONSIN METROPATTERNS: REGIONAL COOPERATION, ECONOMIC GROWTH AND ENVIRONMENTAL PROTECTION* (2002).

11. See generally Jack Stark, *The Authority to Tax in Wisconsin*, 77 MARQ. L. REV. 457, 466 (1994).

12. *The Convention of 1846*, in II WIS. HIST. PUB. COLLECTIONS (Constitutional Series, 1919).

The electorate rejected the constitution, and this language was not included in the 1848 constitution.

The Wisconsin Alliance of Cities has called for a new convention without a predetermined outcome. We believe regional government is an option that our state should consider as part of the debate over a new constitution. Nineteenth century government cannot continue if we are to compete in this "New World" economy. But constitutional conventions do not come easily, and there are many questions that legally need to be answered about what it would take to call a convention in Wisconsin. In some other states that do not have the barriers that Wisconsin has, consolidation and regional government already exist.

V. TO AVOID REGIONAL GOVERNMENT, STATE GOVERNMENT MUST INTERVENE

How do we share revenue regionally without creating a regional government? The answer lies in state government. State government can create regions by legislation. New legislation could require the Department of Revenue to measure income, sales, and property value growth within each of the regions and apply a predetermined rate against the growth. The revenue then could be divided and distributed on a "need" or "equalizing" basis.¹³

The regions could follow the lines of Metropolitan Statistical Areas or, where there are none, combine the remaining counties into a statewide program. The idea is that, in a defined area, everyone has a stake in economic growth. The idea of defining community as a region is not unheard of. The "Valley" in California, "Utopia" in Utah, and Hwy. 128 in Massachusetts are illustrations. Branding and regionally marketing need a thread to bind them together. That thread is regional revenue sharing for local governments.

Many business people do not understand the dynamics of urban decay or the real costs associated with decline. More importantly, it is not understood that the decline is a cancer that starts at the core and works its way outward. It drives taxes up in older areas with higher concentrations of poverty and drives taxes up in newer suburban/ex-urban communities because of redundancy of infrastructure and other marginal costs.

Revenue sharing, at least on a regional level, is essential for every state in

13. Wisconsin could define the natural economic regions where most people live and work as follows: Region one: Douglas County; Region two: Pierce and St. Croix Counties; Region three: Eau Claire and Chippewa Counties; Region four: La Crosse County; Region five: Marathon, Wood, and Portage Counties; Region six: Brown, Winnebago, Calumet, Outagamie, and Fond du Lac Counties; Region Seven: Sheboygan County; Region Eight: Milwaukee, Waukesha, Ozaukee, and Washington Counties; Region Nine: Racine County; Region Ten: Kenosha County; Region Eleven: Dane County; Region Twelve: Rock County.

America. Regional revenue sharing can mitigate the impacts of developmental sprawl and encourage local government leaders to overcome local competition and instead build the region. But it is only part of the picture.

VI. INCLUSIONARY ZONING, REGIONAL LAND USE, AND ECONOMIC PLANNING AND UTILITIES COMPLETE THE PACKAGE

In addition to regional revenue sharing, we need a nongovernmental body to coordinate data collection and planning, assess strengths and weaknesses within any economic region, analyze economic trends, and incorporate goals that can be measured with strategies for implementation. This should be a nongovernmental institution, an institute, if you will, to educate and recommend policy changes that deal with economic development, land use, and inclusionary housing laws.

The fundamental purpose of inclusionary zoning is to allow the development of affordable housing to become an integral part of development. The zoning requirement could be voluntary (offering developer incentives) or mandatory. An inclusionary zoning ordinance would set forth a minimum percentage of units to be provided in a specific residential development that are affordable to households at a given income level, defined as a percentage of the median income of the area.

The key is inclusionary zoning across incomes in every neighborhood. Today we bus students from neighborhood to neighborhood in order to equalize the distribution of poor or minority students within a school district. In Milwaukee, we use vouchers so parents can choose between public and private schools. We do this because we know that poorer income students accomplish greater academic success when exposed to other students.¹⁴

As stated before, systems of local government that do not allow for the freedom of movement within our society by income or race are wrong. Even with revenue sharing and regional marketing, we cannot ignore concentrations of poverty and the impacts on many families. Inclusionary zoning creates better outcomes than government consolidation because it integrates neighborhoods, not cities.

In an editorial by the *Milwaukee Journal Sentinel*, dated September 16, 2002, the Editors asked: "Why not propose regional transportation authority that would cover airports, rail and highways? Or maybe a planning board that could coordinate development across the area? What about creating a

14. David Rusk has done extensive work in this area. See, e.g., DAVID RUSK, *INSIDE GAME/OUTSIDE GAME* 325–26 (1999).

regional authority for the various sports and arts venues in the metropolitan area? What about merging some governments?"¹⁵

Families in Wisconsin (and likely everywhere) really do not care who provides a particular service, only that it be done efficiently and at the least amount of cost to the taxpayer. Contracts between local governments are an effective and politically appealing way of reducing marginal costs. The creation of "utilities" that cross local political lines to provide service is, in a word, doable.

Utilities are another way of accomplishing the outcomes of Samuelson and Tiebout without consolidation of municipal governments. Regional service delivery should be based on capturing economies of scale, not consolidating governments. Elimination of redundancy, which may include mixing private sector with government sector employees, can occur when two or more municipalities create a regional utility.

Creating utilities can increase the use of fees to offset Wisconsin's high property taxes. Only eight states rely on the property tax to a greater extent than Wisconsin for their local revenue. When fees are not counted in comparing state tax burdens, Wisconsin is frequently listed in the top 10 for tax burden. The greater use of fees is a fair way of getting Wisconsin out of the top 10.

Fees must have a close nexus to the service being provided.¹⁶ A fee for services offered, not rendered, as a per square-foot fee for fire service, could significantly reduce property taxes. Services rendered would require that the fee be assessed only if the fire truck came to your house. Services offered means they need only to be available to come to your house. (This would require a legislative change in Wisconsin.) In addition, the fees would shift the burden to all property owners, allowing for discrimination of the fees, based on inventory and height of building, and would relieve homeowners from the subsidization of large institutions and manufacturing properties.

Regional utilities for garbage, recycling, and landfill siting could also bring savings and again be funded by fees. Road plowing and maintenance are other possibilities. Concentrating on service levels and efficiency instead of governmental incorporation allows for total creativity. Consolidation of municipalities is less likely to allow for the kind of creativity that contract law can accommodate.

15. *Why Thinking Big Is Better*, MILW. J. SENTINEL, Sept. 16, 2002, at A10.

16. *Town of Janesville v. Rock County*, 236 Wis. 2d 588, 451 N.W.2d 436 (Ct. App. 1989).

VII. CONCLUSION

If social justice issues and issues such as the “free rider” described by Samuelson are not considered, there are likely to be more calls for (if not more) government consolidation. But it need not be. Both conservatives and liberals should consider the package I have described: *regional revenue sharing, inclusionary zoning, and utility regional service delivery*. Zoning law changes would reduce the need for school busing. Revenue sharing would reduce the need to consolidate or annex property. Regional utilities would reduce property taxes and increase efficient allocation of costs.

In the end, it is not whether Samuelson or Tiebout is right. It is about better government and better service to the taxed public in the twenty-first century.

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