

## RESEARCH SUMMARY

## Local Governments and Economic Freedom: A Test of the Leviathan Hypothesis

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In their 1980 book *The Power to Tax*, economists Geoffrey Brennan and James M. Buchanan introduced the Leviathan hypothesis: the more competing governments there are in an area, the more difficult it will be for them to exploit their constituents. This hypothesis has been tested many times at the country and state levels, but very little work has been done at the local level. It is the local level where residents' mobility, which helps to constrain Leviathan, is highest. City and county governments can also tax constituents and spend money, but do they also behave in an exploitative manner?

In "[Local Governments and Economic Freedom: A Test of the Leviathan Hypothesis](#)," Adam A. Millsap, Bradley K. Hobbs, and Dean Stansel test whether metro area economic freedom increases as local governments become more numerous. The study uses an economic freedom index developed at the metropolitan statistical area (MSA) level as its measure of government exploitation. The study provides the first examination of the relationship between MSA economic freedom and the number of general-purpose governments. The study also controls for a variety of other factors, such as federal aid to state and local governments and regional differences.

Local governments compete with one another for residents and firms, and one way they do this is through local economic and fiscal policy. Since people and firms are mobile, the more competing local governments there are, the harder it is for any particular government to exploit its residents through excessive taxation or to adversely interfere with the economy in other ways.

### KEY FINDINGS

- Economic freedom is positively associated with the number of competing government jurisdictions, with some exceptions in the South and West regions.
- An increase in government competition is associated with an improvement in labor market freedom but has little or no relationship with tax freedom or the size of government.
- As federal transfers to the states increase, labor market freedom decreases, perhaps because of the separation of local revenue from the quality and amount of local government goods and services, which decreases the need for pro-growth economic policies.
- The proportion of adults with a bachelor's degree or more has a positive relationship with overall freedom and labor market freedom, but it has a negative relationship with taxation freedom. Those with more education may be more willing to pay local taxes because of a stronger preference for local government services such as public education.

## REGIONAL FINDINGS

### The Northeast and Midwest

- The Leviathan hypothesis holds: the more competing governments, the more labor market freedom, taxation freedom, and overall economic freedom.
- In states with more laws governing local government, MSAs have less economic freedom on average.

### The South

- The number of local governments has little or no relationship with any of the measures of economic freedom.
- The Leviathan hypothesis does not hold for southern regions where government has historically been more concentrated into county governments.

### The West

- Western governments have historically covered larger areas in order to take advantage of economies of scale when providing services to dispersed populations.
- The number of local governments has little or no relationship with any of the measures of economic freedom.

## CONCLUSION

The study finds evidence that supports the Leviathan hypothesis in metropolitan statistical areas in the Northeast and Midwest but not for those in the South and West. Further research is needed to determine why the results vary by geographic region.