CLAYTON P. GILLETTE

Local Redistribution and Local Democracy

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LOCAL REDISTRIBUTION AND LOCAL DEMOCRACY

For Jordan

PREFACE

This book attempts to merge various but distinct literatures relating to local governments: urban finance theory, public choice theory, and legal theory. Urban finance theory provides us with an ideal of what local governments should seek to accomplish. In one particular conception, it tells us the conditions under which decentralized governments can efficiently provide local public goods and thus gives us a basis for comparing the capabilities of local governments, centralized governments, and markets. Urban finance theory does not necessarily recommend one form of organization over another. There may be reasons to allocate responsibilities to more centralized governments or nongovernmental institutions, notwithstanding the inefficiencies that those allocations engender. Urban finance theory, at least in the form in which I am interested, is silent on those issues.

Public choice theory, however, gives us pause about the teachings of urban finance theory. It tells us that those who are charged with implementing the strategies that allow local governments to achieve what theory tells us they can most efficiently accomplish may deviate from the interests of their constituents. That is, local officials may be unfaithful agents who pursue some personal objective that diverges from pursuit of the public welfare with which they are entrusted. They are aided in this personal effort by collective action problems that induce some parties to

be inattentive to local projects that are not worth their costs, while other parties—often a distinct but well-organized minority—invest heavily in attaining those same projects. The problem of special interests is by no means unique to local government. But local governments may be more vulnerable to the difficulties of special interests for reasons that go back at least to James Madison's observations that decentralized governments are less likely to comprise offsetting factions.

Law can mediate between the teachings of urban finance theory and public choice theory. Law has a positive aspect insofar as it creates rules that allocate responsibilities to certain levels of government. It, therefore, can embody urban finance theory by allocating to localities those functions that are most efficiently delivered at decentralized levels of government. Legal allocations can also implement policies that officials believe should trump efficient provision, such as equitable considerations that may be indicative of a more communitarian vision of local life. But law can also incorporate the lessons of public choice theory and constrain the discretion of officials where circumstances increase the likelihood that officials' conduct will diverge from public welfare. Obviously law can do that in cases of blatant divergence, such as bribery. But legal doctrine may also identify the more subtle circumstances in which local officials can benefit by attending to those most invested in a particular project, notwithstanding that the project fails to serve local interests generally. Law could then raise the costs of official defalcation, either by negating local authority to act autonomously in those circumstances, or by exacting a substantial cost for local action, such as requiring evidence that a particular project comports with local interests. In doing so, law explicitly assigns decision-making responsibility to institutions that are most likely to exercise authority in a manner that reflects the interests of local constituents.

The ability of law to perform this function, however, is complicated by a practical difficulty. Law can proscribe local action in a broad set of circumstances in which deviation from local interests is plausible. But whether any particular project that arguably fits within that description in fact deviates from local interests will likely be contestable. Failure to investigate more deeply the fit between the conditions of divergence from local interests and individual cases risks either weakening the legal threat (if individual cases are presumed to pass muster) or invalidating

projects that would generate significant local benefit (if individual cases are presumed to be invalid). The task of investigating that fit typically falls to courts. But courts suffer from their own issues of institutional legitimacy and competence. Assigning to courts the task of making the necessary individualized determinations essentially asks them to understand the theories of urban finance and public choice that lead to the legal interventions that judges must implement. That raises questions about both the scope of judicial authority and the accuracy with which they can execute the authority they have.

These issues coincide in the puzzle about local government that is central to this book. What I consider here to be the orthodox theory of urban finance predicts that local governments will not engage in the redistribution of wealth. Any effort to do so allegedly will induce those who are net subsidizers of redistribution to exit and will attract those who can benefit from redistribution. Thus, a locality that attempts to redistribute wealth will soon discover that it has lost tax base that it needs to provide services to residents and that it has gained a significant population that cannot pay the tax price that corresponds to the locally provided benefits that the population consumes. Notwithstanding that very basic assumption of urban finance, virtually every major locality engages in the redistribution of wealth. The objective of this book is to explain that apparent contradiction and to indicate the role that law can play in resolving it. Law assumes that role because, as one achieves a richer understanding of local motives in redistributing wealth, the resolution may lie in either a relatively happy story in which the apparent contradiction disappears, or a relatively unhappy story in which, consistent with public choice theory, the contradiction is attributed to divergence between the interests of local residents and of the officials who are charged with serving those interests. Law and legal institutions play a role in distinguishing between these explanations.

It is possible, of course, indeed likely, that each of these explanations accounts for some part of the local redistribution puzzle. That is where the practical issues related to law step in. Ideally, law might be able to instantiate the richer understandings of local motives, so that localities that have benevolent reasons for redistribution, emanating from local self-interest or altruism, would be authorized to act, while those that redistribute for more nefarious motives, such as serving the personal goals of officials,

would be constrained. Can law effectively play that role? That is, can legal institutions, primarily courts that would be asked to challenge redistributive programs, isolate those situations in which redistribution is inappropriate, while validating those situations that serve local welfare or local preferences? These inquiries motivate this book. I am, therefore, interested in issues of institutional design. Urban finance theory tells us that one level of government rather than another is best situated to serve particular functions. Public choice theory tells us that different institutions may suffer different degrees of agency costs and that one way to control agency costs related to one institution is to subject its decisions to review by an alternative institution. Legal theory allows us to develop rules that optimize decision-making responsibilities and define the circumstances and design of reviewing institutions.

This book draws on much of my prior work. Some of the basic ideas were set forth in an article, "Local Redistribution, Living Wage Ordinances, and Judicial Intervention," published in the *Northwestern University Law Review* in 2007. I am grateful to the *Law Review* for publishing that piece and for recognizing that it would subsequently be the subject of further development. I am also grateful to a variety of colleagues who discussed many of the ideas that appear in this book, though none of them should be tarred with the accusation that they agree with me. They include Ed Baker, Lynn Baker, David Barron, Vicki Been, Richard Briffault, Helen Hershkoff, Rick Hills, Marcel Kahan, Lewis Kornhauser, Daryl Levinson, Gerald Lopez, Rick Pildes, Richard Revesz, Julie Roin, Richard Schragger, Dan Shaviro, and participants in workshops at New York University School of Law, the University of Florida College of Law, and Florida State University College of Law. Student assistants at NYU School of Law were also instrumental in gathering some of the material on which I relied. Ben Holzer of the NYU School of Law Class of 2009 was particularly helpful, especially with respect to the history of municipal poor relief. Dean Richard Revesz generously permitted me a sabbatical to put many of these thoughts together. The Filomen D'Agostino and Max E. Greenberg Research Fund at NYU School of Law provided generous research support. This book would not have come to fruition without the encouragement and support of Michael O'Malley of Yale University Press. Ann-Marie Imbornoni's close reading and edit of the manuscript caused me to correct and clarify

much of the text. Of course, my greatest gratitude is reserved for Abby Gillette for bearing all the standard obligations and sacrifices that we impose on those to whom we are closest, and then for so much more.

Prior to writing this article I served as a consultant to opponents of some of the living wage ordinances mentioned in this article and was a signatory on an amicus brief supporting another living wage ordinance. Perhaps those seemingly inconsistent roles reflect the complexity of the analysis that I discuss herein.

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CHAPTER ONE

The Scope of Local Competence

IN JULY 2006, the Chicago City Council brought what it likely thought was a climactic conclusion to a controversial proposal that required a few local employers to pay their workers a "living wage." The 35 to 14 vote increased the minimum wage payable by covered employers to $10 per hour, plus $3 in benefits per hour, by July 2010. The new wage represented a substantial increase over the then-applicable federal minimum of $5.15 per hour and even exceeded the Illinois statewide minimum wage, which was scheduled to reach only $8.25 by the time the ordinance became effective. Primary proponents of the ordinance—including labor organizers; the Grassroots Collaborative, which consisted of local church and labor leaders; and ACORN, a national organizing group—maintained that its enactment would remedy exploitation of the working poor, reverse what advocates labeled as "callous disregard for hard-working people,"[1] and fetter corporations whose workplace practices allegedly frustrated employees' effort to enter the ranks of the middle class.

But the city council's effort to improve the lot of local employees had limited scope. The ordinance would apply only to those employers described in the ordinance as "large retailers." That term comprised retail stores in the city that occupied ninety thousand square feet or more, and that were part of a company that had total annual gross revenues of $1 billion or more. In short, the ordinance was directed at "big-box"

stores, for which Wal-Mart and Home Depot have served as poster children. While opponents of the proposal contended that living wage ordinances were inherently antibusiness and would cause Chicago to lose badly needed jobs and tax revenue to suburbs more hospitable to national retailers, at least some opponents also questioned what they saw as discrimination against big-box employers and promised legal challenges once the ordinance passed.

The immediate targets of the proposal strategically remained on the sidelines during much of the debate, although Wal-Mart had recently indicated an interest in opening a new store on Chicago's relatively poor South Side. Instead, local proxies ensured that the chains' views were heard. Local suppliers and small businesses that performed work for the big-box stores testified against the ordinance. After the vote approving the ordinance, however, Wal-Mart officials themselves became more vocal. They indicated that the wage ordinance would "make it hard to invest in Chicago"[2] and announced a strategy of serving Chicago residents "from suburban Chicagoland."[3] Target Corp. was reported to have placed "on hold" plans to open additional stores in the city and to be considering closure of its existing stores.[4]

Nevertheless, the proponents celebrated the vote as a major victory in nationwide efforts to enact living wage ordinances. While some form of minimum wage requirement had been enacted in more than 120 cities and counties, most were smaller localities, and most of the ordinances extended the applicable wage only to municipal employees or employees of suppliers that contracted directly with the locality. An ordinance in a major city that applied to private employers promised to change the terms of the debate.

Alas, the proponents' celebration was short-lived. In mid-September, Mayor Richard M. Daley exercised his veto authority for the first time in his seventeen years in office. In his brief letter of explanation to the city council, Daley contended that the ordinance "would drive jobs and businesses from our city, penalizing neighborhoods that need additional economic activity the most." Daley concluded that it was his "duty" to veto the ordinance.[5]

Daley's response was not unexpected. He had earlier announced his opposition to the ordinance and had lobbied against its adoption. But proponents had declared the margin of victory "veto-proof." They had

miscalculated. Largely at Daley's instigation, three aldermen who had initially supported the measure voted against overriding the veto. One of the converts represented a district on the South Side where Wal-Mart had indicated it might locate its first Chicago store; the other two had close ties to the Daley political organization. Two weeks after the veto, Wal-Mart opened its first Chicago store, located on the relatively poor West Side of the city.

The living wage issue did not disappear with the mayor's victory. In the following year's city elections, the Chicago Federation of Labor failed to endorse the incumbent mayor for the first time in its history. Instead, organized labor worked to defeat the aldermen who had voted against the measure. In February 2007, eleven incumbent aldermen failed to obtain the majority vote necessary to avoid a runoff election in their districts. Many cited their failure to support the big-box ordinance as a cause of their electoral difficulties. In the subsequent elections, a half dozen aldermen aligned with the mayor on the living wage ordinance were defeated by union-backed candidates. The signal was clear: the living wage ordinance was on the exam in the course of local politics, and those who opposed it had failed.

The intensity of the Chicago debate was not unprecedented. In 2001, the city council in Santa Monica, California, had passed a living wage ordinance that required covered employers to pay employees $10.50 per hour plus benefits or $12.25 per hour without benefits. Although the Santa Monica ordinance was not as narrowly drawn as Chicago's, it did not target all local employers. It applied to the city with respect to its own employees, to any contractor or subcontractor with respect to workers on projects performed under contract with the city, and to any private employer whose business met a gross receipts test and was located in an area of the city designated as the Coastal Zone or Extended Downtown Core. The restrictions on gross receipts and location limited the private employers who were subject to the ordinance primarily to hotels and restaurants along the Santa Monica beachfront. The ordinance also contained a clause that rendered it inapplicable to wage rates established through a collective bargaining agreement, as long as that agreement specified that it was intended to supersede the wages set forth in the ordinance.

In heated exchanges before the Santa Monica City Council, proponents of the ordinance defended the need to pay a living wage to

low-wage workers, many of whom were immigrants and nonresidents of the city. Local business owners contended that the ordinance would cause them to reduce their workforce, thus hurting the very class of individuals proponents purported to assist. Labor activists and union members featured prominently among the advocates of the ordinance, while the affected hotel owners were instrumental in organizing the opposition. After the city council enacted the law, many of the approximately forty firms subject to its private business provision organized a referendum campaign to place the issue in front of the electorate. In the ensuing November 2002 plebiscite, a narrow majority—14,380 to 13,860—rejected the ordinance.[6] There the story remained for about two and a half years. Then, in early 2005, the city council enacted another living wage ordinance. This version, however, covered only employees of private contractors who entered into contracts of $50,000 or more with the city itself. Neither city employees nor employees of the private firms that had opposed the earlier ordinance were subject to the new proposal. The modified ordinance became effective on July 1, 2005.

Santa Fe, New Mexico, witnessed a similarly contentious path for a living wage ordinance but experienced a different result. In 2003, the city council considered expanding an existing ordinance that required payment of higher than otherwise applicable minimum wages to city employees, contractors doing business with the city, and other businesses directly receiving benefits from the city. As initially introduced, the proposed ordinance both increased the applicable minimum wage and extended the scope of the ordinance to cover all for-profit employers in the city that had more than ten employees and nonprofit businesses that employed more than twenty-five workers. The proposed wage would start at $10.50 per hour in 2008, with subsequent increases tied to the consumer price index for urban wage earners in the western United States. Approximately 75 percent of all employees and 20 percent of all businesses in Santa Fe would have been subject to that version of the ordinance.

At a public hearing that lasted into the early morning hours of February 27, economists, members of the Green Party of Santa Fe, labor activists, advocates for the working poor, and workers faced off against small-business owners, representatives of the New Mexico Restaurant Association, officers of nonprofits, and hotel managers. Seventy-three

people spoke in favor of the ordinance, eighty-five against it. In emotional terms that touched on the political, economic, and social implications of the issue, advocates emphasized the low costs that the ordinance entailed, the moral issues involved in ensuring payment of a living wage, and the economic distress of the working poor. In similarly evocative terms, opponents stressed the risk of shuttered small businesses, the difficulty of finding workers whose productivity warranted higher-than-market wages, and the disincentives that the ordinance would create for businesses to locate in Santa Fe.[7] City councilors enacted the ordinance by a 7 to 1 vote, but only after it had been narrowed to cover employers with twenty-five or more workers. The amendments reduced the coverage of the ordinance to about 60 percent of the Santa Fe workforce and cut in half the number of small businesses that would be affected.

Enactment of the Santa Fe ordinance generated the inevitable lawsuit. The challengers contended that Santa Fe lacked legal authority to adopt a local minimum wage. Under well-established, if controversial, legal principles, local governments lack the capacity to initiate local legislation without prior legislative or state constitutional authority. Local governments are, in the standard language of legal doctrine, merely political subdivisions of the state, which exercises plenary power over them. As a corollary of these principles of limited municipal autonomy, any conflicts between state laws and local ordinances are typically resolved in favor of the former. The challengers contended that Santa Fe's ordinance exceeded the permissible scope of local legislation. Both the trial court and the court of appeals dismissed the objections.[8] Santa Fe was a "home rule" municipality, which, under the state constitution, enabled it to enact legislation relating to "local affairs" without a prior explicit grant of authority from the state. The living wage ordinance, the courts concluded, fell within that protected domain. Even a home rule locality is generally disabled from enacting legislation that directly conflicts with state laws. But, the courts declared, the state's minimum wage law, which imposed a lower hourly rate than the one dictated by Santa Fe, was intended only to set a floor, not a ceiling. Thus, the local ordinance was neither inconsistent with nor superseded by state law.

As evidenced by the broad array of cities and counties that have adopted living wage ordinances, the debates in Chicago, Santa Monica, and Santa Fe do not represent exceptional episodes. The campaigns in

these municipalities, however, do demonstrate the passion and politics that local proposals for redistributing wealth can generate. Embodied in these controversies are deeply varying ideologies about the economic effects of wage rates, governmental intervention into labor markets, the widening income disparity between wealthy and poor, and the proper scope of local government. Something less noticed but of equal importance is that the controversies over living wage ordinances reveal the various political forums in which decisions about controversial proposals for local action can occur. While organized proponents may effectively lobby for enactment of the proposals before local legislatures, *organized* opponents may similarly appeal to local representatives or seek to reverse legislative decisions through referenda, state intervention, or litigation. Different forums, these examples indicate, may generate different results, so that the enactment or defeat of a proposal may ultimately appear to be a consequence of the arena in which the determination was made, rather than of any inexorably correct view of the proper scope of local action.

My concern in this book is with the particular set of biases that judicial determinations bring to the process of defining the scope of local autonomy. As the Santa Fe situation reveals, litigation, like war, can be a continuation of politics by other means. Where enactment of living wage ordinances has generated litigation, the judicial responses to the legal issues have been as mixed as legislative responses to the explicitly political ones. The Louisiana Supreme Court invalidated a New Orleans living wage law by finding violations of the same type of state constitutional requirements that the New Mexico courts had found to be satisfied.[9] A Missouri appellate court similarly held that state law preempted a St. Louis proposal.[10] But a New Jersey appellate court upheld a county living-wage ordinance against challenges on equal protection and vagueness grounds,[11] and a deeply divided panel of a federal appellate court rejected a federal constitutional challenge to a living wage ordinance in Berkeley, California.[12]

The Louisiana Supreme Court decision most thoroughly considers the legal doctrines through which the underlying tensions are displayed. In four different opinions, that court debated the scope of autonomy that home rule municipalities enjoy, the extent to which local wage ordinances generate statewide effects that preclude municipal regulation, the capacity of localities to regulate private economic activity, and the appropriate role