

# Leviathan or Public Steward? Evidence on Local Government Taxing Behavior from New York State

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Fiscal federalism argues local governments compete to provide optimal tax-service bundles as responsible public stewards. In contrast, Leviathan theories argue tax and expenditure limitations (TEs) are necessary to make local governments fiscally responsible. We analyze local taxing behavior in New York State, which implemented a levy limit in 2012 that allows legislative overrides with 60 percent vote of the local governing board. Our 2017 survey of all general-purpose local governments measured fiscal stress, service responses, and local political attitudes and found 38 percent of municipalities voted to override. Logistic regressions show local governments that have more fiscal stress, weaker property tax bases, higher need, and higher employee benefit costs are more likely to override. These findings support fiscal federalism, as local governments that override are pushing back against state policy in order to respond to local needs. TEs introduce unnecessary rigidity and run counter to the precepts of fiscal federalism.

The U.S. government structure is highly decentralized, based on theories of fiscal federalism that argue a federal system is efficient and effective. The diverse and numerous local governments that pursue development (Musgrave 1959; Peterson 1981) and compete to provide the best tax-service bundle are considered key institutions in this system (Oates 1972; Tiebout 1956). However, recent trends in state-local relations show increasing mandate burdens, decreasing local revenue authority, and growing state preemption of local policy authority (Kim and Warner 2018b; NACo 2016; NLC 2017; Riverstone-Newell 2017). Recent empirical research finds these shifts in state-local relations may reduce the developmental role of local governments (Xu and Warner 2016) and their ability to respond to local needs (Xu and Warner 2015)—potentially signaling a crisis of fiscal federalism (Peck 2014).

The concern of whether local governments respond to local needs is not new. The Public Choice literature has warned about the dangers of a Leviathan government expanding its budget above and beyond the preferences of citizens (Brennan and Buchanan 1979). The Leviathan view is particularly skeptical of *local* governments in a federal system making responsible budget decisions, because local governments may believe higher levels of government will bail them out (the “soft budget problem”; Kornai 1986; Qian and Roland 1998). This skepticism, in turn, has formed the theoretical support for constitutional and/or statutory limits on local budgets called tax and expenditure limitations (TEs) (Stallmann et al. 2017). While fiscal federalism believes that local governments will focus on development (Musgrave 1959; Peterson 1981) and behave in fiscally responsible ways to offer optimal tax-service bundles (Oates 1972; Tiebout 1956), state-imposed TEs are based on the belief that the pressures in a federal system are inadequate to check Leviathan behavior at the local level. In the post-Great Recession world, this skepticism has supported some radical state takeovers of local governments (e.g., Michigan’s Emergency Management Laws; Anderson 2012).

Does fiscal federalism still hold? Or are TEs necessary to force local governments to act as good stewards of public resources? We use local government overrides of a recently implemented TE in New York State (NYS) to gain insights into the taxing behavior of local governments. This is a good opportunity to observe local government taxing behavior for two reasons. First, New York’s TE is different from ones in other states. It is relatively flexible in that legislative overrides of the constraint only require a 60 percent vote of the governing board, rather than a public referendum (Wen et al. 2018). This makes the override decision a proxy measure for the taxing behavior of local governments. Second, New York’s TE is a levy limit that constrains the annual growth of the total amount of property tax collected. This means the override decisions reflect local government choices about the total budget from property taxes (rather than just the tax rate or assessment behaviors) and this creates a test for Leviathan behavior (if any).

Fiscal federalism is based on a multilevel structure that creates pressures for efficiency from above (including fiscal and political pressures from the states), from below (pressures from local voters), and laterally (competition with other local governments). To capture these various pressures, we conducted a state-wide survey of all general-purpose local governments (excluding New York City, which is exempt from the TE) in NYS in 2017. A logistic regression analysis shows fiscal responsibility drives levy limit overrides, rather than Leviathan behavior. Upstate jurisdictions with greater fiscal stress, developmental expenditure needs (road repair), weaker property tax bases, and high employee benefit costs (largely determined by state legislation) are more likely to override. These results show

fiscal federalism still holds, but raise the question of whether a levy limit is necessary. We return to this question at the end of the article and argue that TELs may introduce an unnecessary rigidity that decreases efficiency at the local level in a dynamic federal system.

## **Fiscal Federalism, Local Taxation Behavior, and Tax and Expenditure Limitations**

We contrast two theoretical lenses to understand local government taxation behavior: Fiscal Federalism and the Leviathan/Public Choice view. Fiscal federalism argues that in a decentralized system of governments, local governments tax and spend per local preferences, resulting in more efficiency and effectiveness (Drew and Grant 2017; Olson 1969; Oates 1972; Tiebout 1956). The assumptions are that local governments pursue development (Musgrave 1959; Peterson 1981), compete to offer the best tax-service bundle (Oates 1972; Tiebout 1956), and that the spatial benefit and cost of services match (“fiscal equivalence”; Olson 1969). The implicit assumptions are that local governments behave in fiscally responsible ways and that the pressures from a multilevel governance structure (from higher-level governments above and citizen-voters below) keep the system efficient and effective (Homsy et al. 2018; Warner and Clifton 2014). The Leviathan/Public Choice view, by contrast, argues local officials engage in budget-maximizing behavior to capitalize on their individual interests (Brennan and Buchanan 1979; Tullock 1959). This view assumes the multilevel pressures are inadequate to check these Leviathan tendencies, making TELs necessary.

TELs are widespread (in forty-seven states; Wen et al. 2018), but are they necessary? Past research found local governments under TELs had higher reliance on fees and charges (McCubbins and Moule 2010; Shadbegian 1999), and create more special taxing districts (Carr and Farmer 2011). Whether these efforts to “get around” TELs are driven by Leviathan tendencies or to meet service needs/citizen preferences is unclear. Moreover, recent research is finding opposite results. For example, using over forty years of data on contiguous counties, Goodman (2018) found stringency of TELs has a weak relationship to higher usage of special districts, and Wang (2018) and Kim (2017) found cities with more stringent TELs do not rely more on charges and fees. In fact, in a review of TEL impact studies, Stallmann et al. (2017) conclude, “TELs seldom have the intended outcome their proponents promise” (p. 213). These promises include disciplining local government Leviathans (as public choice theories argue) and increasing responsiveness to local preferences.

Most TELs require voter approval through referenda for overrides, and only four states (Louisiana, Maine, New York, and West Virginia) allow legislative overrides (Wen et al. 2018). Studies of TEL overrides by referendum find overrides

are common for stringent TELs. For example, [Roscoe \(2014\)](#) found between 1990 and 2007, 82 percent of localities attempted an override of Proposition 2 1/2 in Massachusetts and [Maher et al. \(2017\)](#) found 1744 public referenda to override TABOR between 1993 and 2014 in Colorado.

When the override decision is up to the local governing board (as in NYS), the decision is easier in theory, but still has high political costs ([Kim 2018](#)), especially in the post-Great Recession context of fiscal stress and high anti-tax sentiments ([Pagano et al. 2012](#); [Peck 2014](#)). As fiscal stress in the public sector increases, scholars note U.S. federalism has shifted from a cooperative or functional model (wherein states focus on redistribution and local governments focus on development) to a hyper-competitive or fend-for-yourself federalism in which states compete with local governments over development and push down redistributive responsibility to the local level ([Gamkhar and Pickerill 2012](#); [Nicholson-Crotty and Theobald 2011](#); [Xu and Warner 2015](#); [2016](#)). If local officials are maximizing self-interest as public choice theories suggest, then they would override regardless of any fiscal stress. If local officials are fiscally responsible, then fiscal stress may encourage them to override a TEL in order to fulfill their developmental role, respond to citizen need, and achieve fiscal equivalence—the promises of fiscal federalism.

Indeed research since the Great Recession finds U.S. local governments are practicing “pragmatic municipalism” ([Kim and Warner 2016](#)), attempting to respond to fiscal stress with service innovation to avoid cutbacks. But there is geographic variation in local government responses with suburban localities more likely to pursue privatization and intermunicipal cooperation than urban and rural localities ([Kim and Warner 2018a](#); [Hefetz et al. 2012](#)). Some communities are hollowing out services while others are “riding the wave” and exploring new forms of service innovation to meet needs ([Warner and Clifton 2014](#)). A National League of Cities survey finds cities have begun cutting back on longer term infrastructure projects ([Pagano et al. 2012](#)) because infrastructure spending is easier to delay than current spending. But this can harm the future growth potential of communities because public infrastructure investment is a key driver of growth ([Reese 2012](#)). If local officials are fiscally responsible, then low economic growth and the erosion of infrastructure spending may prompt them to override a TEL in order to maintain their developmental responsibilities.

Fiscal federalism theories recommend local governments rely on the property tax because of its efficiency and stability ([Musgrave 1959](#)), but [Pagano and Johnston \(2000\)](#) found in a study of 1,087 local governments that property tax dependence is related to weaker budget capacity. Moreover, the property tax is politically unpopular, and as the new economy is centered on “eds and meds” (e.g., universities and hospitals), which often are exempt from property taxes, this revenue source may be inadequate for funding local services ([Bartle et al. 2011](#)).

In a study of 2,396 cities after the Great Recession, [Kim \(2017\)](#) found cities with higher service needs but lower home values rely more on charges and fees. A Leviathan government may try to shift the budget structure away from property taxes (a highly visible tax) and toward charges and fees to expand its budget without raising residents' attention ([Wagner 1976](#)). But under fiscal federalism, local governments will try to minimize the *overall* fiscal burden on residents by avoiding tax increases while meeting service needs. Thus, we may expect property tax dependence to have no direct relationship to TEL overrides, while localities with higher overall tax effort may be less likely to override a TEL. The goal of meeting service needs may, in turn, encourage localities with more property tax exemptions due to “eds and meds” to be more likely to override TELs.

While fiscal federalism celebrates the benefits of competition among local governments, there is also the challenge of achieving fiscal equivalence in a fragmented system. Metropolitan regions are becoming important economic engines, as central cities function within a regional network ([Katz and Bradley 2013](#)). The high degree of municipal fragmentation in metro regions undermines political cohesion ([Berry 2009](#)), and suburban jurisdictions have been shown to free ride on amenities of the core city ([Homsy and Warner 2015](#); [Kantor and Nelles 2015](#)). Fiscal equivalence is a key principle of fiscal federalism ([Sorens 2011](#)), and fiscal federalism recommends intergovernmental aid as a solution ([Warner 2001](#); [Olson 1969](#)). Thus, state-level policies are crucial for fiscal federalism to work. However, state governments may devolve their own stress down to the local level through cuts in state aid and decentralization of expenditures ([Pagano et al. 2012](#)) and use political power to blame local governments for fiscal stress ([Hinkley 2017](#); [Kim 2018](#); [Peck 2014](#)) and restrict local authority ([Kim and Warner 2018b](#)). In a spatial analysis of U.S. county areas between 2002 and 2007, [Xu and Warner \(2016\)](#) found these state policies may be “crowding out” the developmental role of local governments.

As mentioned before, the rationale for TELs is based on the assumption of more fiscal responsibility from voters, and thus most TELs put override decisions in the hands of voters ([Wen et al. 2018](#)). Studies of TEL overrides have applied the Median Voter Theorem and found that demography is a strong determinant of voter support for both TELs and override referendums ([Ladd 1978](#); [Ladd and Wilson 1983](#); [Lowery and Sigelman 1981](#)). These studies generally find voters who are white, older, less educated, desire lower taxes, and identify as conservative have a higher propensity of supporting TELs. However, whether tying local budget decisions to referenda leads to more fiscally responsible outcomes is unclear, especially when participation in local elections is often dominated by special interest groups ([Anzia 2014](#)). Our study focuses on the attitudes and actions of local legislative councils and provides a test of

the relative explanatory power of Fiscal Federalism or Leviathan/Public Choice theories.

## Method of Analysis

In order to understand local taxation behavior, we model local government overrides of a state-imposed levy limit in NYS as a function of structural and local variables that include fiscal, economic, demographic, and political elements. We are able to probe the importance of local governing board attitudes to test the relative importance of fiscal federalism or public choice “Leviathan” notions of local government behavior.

In 2012, the New York State Legislature implemented a property tax levy limit (“tax cap”) on all local governments, except for NYC. The tax cap limits the annual growth in property tax *levy* to either 2 percent or the rate of inflation, whichever value is less. The tax cap was championed by Governor Andrew Cuomo who argued property taxes in the state are “out of control” and local governments in NYS are “wasteful and very, very expensive” (Cuomo 2011). In addition, the Governor initiated a Tax Freeze Rebate program encouraging local governments to submit efficiency plans and promising taxpayers a rebate if their government stayed under the cap. However, data show property taxes in NYS were flat in real terms even before the tax cap (Kim 2018). Research has shown that other state governments have used similar narratives of local government failure and inefficiency to shift blame for fiscal stress (Hinkley 2017). Because local governments in NYS can override the tax cap with 60 percent of the governing board votes, this creates an opportunity to observe taxation behavior of local governing boards.

## Data

Our primary data come from a state-wide online survey (“our survey”) we conducted in spring 2017—five years after the tax cap was first imposed in 2012. We designed the survey based on focus groups with local government officials held in 2015 that helped identify the factors to measure (Kim 2018). The survey was administered in collaboration with the NYS Conference of Mayors and Municipal Officials and the Association of Towns of the State of New York. The survey included questions regarding the fiscal stress of each jurisdiction, drivers of that stress, governing board attitudes, service delivery, and responses to state actions. Respondents were either the chief elected or administrative officer from cities, counties, towns, and villages in NYS. For a report on the survey, see Aldag et al. (2017).

Of the 1,596 units of general-purpose local government in NYS, 919 responded to the survey, representing a 58 percent response rate. All government types are

well represented in the sample: 76 percent of sixty-two cities, 53 percent of fifty-seven counties, 55 percent of nine hundred thirty-two towns, and 61 percent of the five hundred forty-five villages. The survey data were linked to data from the American Community Survey (5-year averages for 2005–2009 and 2011–2015) and local budget and fiscal stress data from the Office of the NYS Comptroller for Fiscal Year 2015 (the most recent comprehensive data available). Our final dataset is comprised of 609 cases with complete information from our survey, the ACS, and the NYS Comptroller data.<sup>1</sup>

### **Dependent Variable: Overrides**

The dependent variable is a binary variable that measures whether the jurisdiction overrode the tax cap in the last three years. Thirty-eight percent of respondents indicated that they overrode the tax cap. Compared to studies of TEL overrides in other states, this is a lower rate. Recall that overrides in NYS are “easier” because it is a local legislative action, rather than a popular referendum.

To gain further insights on local government decisions to override, the survey asked why or why not localities overrode the tax cap (table 1). Respondents could choose multiple reasons, and the answers for overriding were: “To be able to maintain services” (72 percent), “To cover increases in costs of employee benefits<sup>2</sup> (e.g., pensions and health insurance)” (60 percent), “To be able to maintain long term capital investments” (40 percent), and “Uncertainty in budget projections (e.g., Comptroller’s growth factor determination or potential mathematical errors in calculating levy limit)” (33 percent). The most popular reasons show local governments seek to respond to local need and fulfill their developmental role. Reasons for not overriding (multiple answers possible) included: “Was not necessary to meet budget needs” (60 percent), “In order for residents to qualify for the Tax Freeze Rebate” (55 percent), “Voters oppose idea of override” (21 percent), and “Fear of retribution from state government” (18 percent). The Tax Freeze Rebate program was implemented by the Governor to increase citizen pressure on local governments to stay under the tax cap. The program provided a state rebate on property taxes if the local government stayed under the tax cap and submitted a government efficiency plan. The most popular reasons for not overriding the tax cap suggest overrides are not due to localities over-taxing in a Leviathan fashion. Instead, these responses suggest local leaders are pragmatic and override primarily to respond to community needs.

### **Independent Variables**

Our independent variables include fiscal/economic, political, and demographic measures at both the structural level (i.e., largely outside of local government control) and local level.

**Table 1.** Motivators to override or not override the New York state tax cap

	Percent yes
<i>Why did your jurisdiction override the tax cap? (N=330)</i>	
To be able to maintain services	72
To cover increases in costs of employee benefits	60
To be able to maintain long term capital investments	40
Uncertainty in budget projections	33
<i>Why did your jurisdiction not override the tax cap? (N=548)</i>	
Was not necessary to meet budget needs	60
In order for residents to qualify for the tax freeze rebate	55
Voters oppose idea of override	21
Fear of retribution from the state government	18

Source: New York State Local Government Fiscal Stress Survey (2017),  $N = 878$ , New York State local governments.

### ***Fiscal and economic variables***

We use two measures of fiscal stress. The first is a structural measure from the 2016 NYS Comptroller Fiscal Stress Monitoring System that assigns fiscal stress scores (scale of 0–100) for all local governments based on fund balances, operating deficits, cash positions, and outstanding debt. The most recent 2016 report shows forty of the 1596 general-purpose local governments (2.5 percent) in the state have either “moderate” or “significant” fiscal stress. Local officials may be able to look beyond budget numbers and have a more comprehensive understanding of local fiscal stress for their jurisdiction. The second measure of fiscal stress is a local measure from our survey question, “In your opinion, what is your jurisdiction’s level of fiscal stress?” Respondents ranked their stress on the following scale: “none” (1), “weak” (2), “moderate” (3), and “significant” (4). Compared to the Comptroller’s measure, 46 percent of survey respondents indicated they have either “moderate” or “significant” stress (average = 2.4; table 2). If local officials are fiscally responsible as fiscal federalism predicts, we expect localities under more stress are more likely to override the tax cap to meet service needs.

We include three measures that relate to the property tax. The first is a structural measure of property tax dependence (property tax revenue divided by total locally raised revenue; 2015 NYS Comptroller Financial Data). We also include a measure of property taxing effort (total property tax revenue divided by the total assessed value of each jurisdiction; 2015 NYS Comptroller Financial Data). We expect localities with higher property taxing effort will be less likely to override the tax cap. Lastly, we include local officials’ perception of tax exempt



**Table 2.** Descriptive statistics of model variables, New York state local governments

	N	Mean	SD	Min	Max
Tax cap override (binary, yes = 1) <sup>a</sup>	878	0.38	0.48	0	1
<i>Structural variables</i>					
<i>Fiscal/economic</i>					
Comptroller fiscal stress rating <sup>b</sup>	868	11.8	11.9	0	75.8
Employee benefits as % expenditure <sup>c</sup>	904	14.4	5.9	0.7	35.4
Property tax dependence <sup>c</sup>	903	51	22.4	0.8	98.8
Employment change (%) <sup>d,e</sup>	919	-0.5	5.8	-78.6	40.4
<i>Demographic</i>					
ln (Population) <sup>d</sup>	919	8.1	1.4	1.8	13.8
Poverty (%) <sup>d</sup>	919	12.4	6.7	0	44.8
College educated (%) <sup>d</sup>	919	27.6	15.9	4.4	100
Above 65 (%) <sup>d</sup>	919	17.2	5.6	2.1	56.6
NYC suburban region (dummy, yes=1) <sup>d</sup>	919	0.2	0.4	0	1
<i>Local response variables</i>					
<i>Fiscal/service delivery</i>					
Local perceptions of fiscal stress <sup>a</sup>	766	2.4	0.9	1	4
Tax exempt land contribution to fiscal stress <sup>a</sup>	871	2.7	0.9	1	4
Property taxing effort <sup>a</sup>	919	0.6	0.4	0	2.5
Cutback in road repair (dummy, yes=1) <sup>a</sup>	836	0.3	0.5	0	1
Total services provided <sup>a</sup>	919	8.2	4.7	1	21
<i>Political Variables</i>					
Liberal governing board (dummy, yes=1) <sup>a</sup>	907	0.1	0.2	0	1
Pushback against Governor's narrative <sup>a</sup>	798	4	1.3	1	5
Believe local inefficiency narrative <sup>a</sup>	799	1.8	1.2	1	5
Submitted government efficiency plan (dummy, yes=1) <sup>a</sup>	845	0.6	0.5	0	1

Sources: <sup>a</sup>New York State Local Government Fiscal Stress Survey (2017), <sup>b</sup>New York State Comptroller Fiscal Stress Monitoring System (2016); <sup>c</sup>New York State Comptroller Financial Data on Local Governments (2015); <sup>d</sup>American Community Survey 5-year estimates (2011–2015), <sup>e</sup>American Community Survey 5-year estimates (2005–2009).

land's contribution to fiscal stress (our survey). We asked respondents how much tax-exempt properties contributed to their fiscal stress on a 4-point scale of "none" = 1, "weak" = 2, "moderate" = 3, and "significant" = 4. The average is "moderate" (mean = 2.7). If local officials are fiscally responsible, they should recognize that weaker property tax bases call for more revenues to fund services, and thus may be more likely to override the cap.

During our focus groups, local officials mentioned employee benefits as a big cost-driver, and the inability of local governments to change these costs due to

state legislation (Kim 2018). NYS has relatively strong union protections based on the Taylor Law and Triborough Amendment that require binding arbitration and thus limit local government control over employee benefits. Recall 60 percent of overriding jurisdictions indicated they did so to “cover the increasing costs for employee benefits.” We include a structural measure of the percentage of total expenditure attributed to employee benefits (local expenditures on employee benefits divided by total local expenditure; 2015 NYS Comptroller Financial Data). We expect places with a larger portion of employee benefits as a percent of total expenditure to be more likely to override the tax cap.

We also include a structural measure of economic performance, the percentage change in employment (2005–2009 and 2011–2015 ACS). A negative number indicates decline in employment (or “economic decline”) and a positive number indicates increase in employment (or “economic growth”). On average, there was economic decline in NYS. If local governments are playing a developmental role, then localities with economic decline are more likely to override the tax cap.

According to fiscal federalism, local governments pursue economic growth and developmental expenditures. But cutting back on infrastructure spending was a widespread response to fiscal stress after the Great Recession (Pagano et al. 2012). Our survey asked local government officials if they “cut back services in response to fiscal stress?” and 28 percent indicated they made cuts in road repair. This was the service most likely to be cut back of the twenty-one measured on the survey. In the model, a dummy variable indicates if cuts were made in road repair (cuts made = 1; otherwise = 0). Because cuts in infrastructure directly erode their developmental role, we expect localities that made cuts in road repair will be more likely to override the tax cap.

We also include the total number of services a government provides, as governments with more service responsibilities might be more likely to override the tax cap to maintain the service mix their citizen’s expect. Maintaining services was a primary reason for legislative overrides (recall Table 1) and this supports fiscal federalism’s principle of local governments trying to provide the best tax-service bundle. The survey measured twenty-one of the most commonly provided services in the following categories: public works and public transit, public safety, health and human services, and economic development, planning, and public relations.

### ***Political variables***

Previous studies of voter-approved TEL overrides found voters’ political ideology drives the outcomes (e.g., Ladd 1978; Ladd and Wilson 1983; Lowery and Sigelman 1981). However, if local officials are making taxing decisions based on fiscal responsibility, political ideology should not affect tax cap overrides. Our survey asked respondents to indicate if their governing board is predominantly liberal, predominantly conservative, or mixed. We include a dummy variable in the model indicating if the governing board of the locality was predominantly liberal.

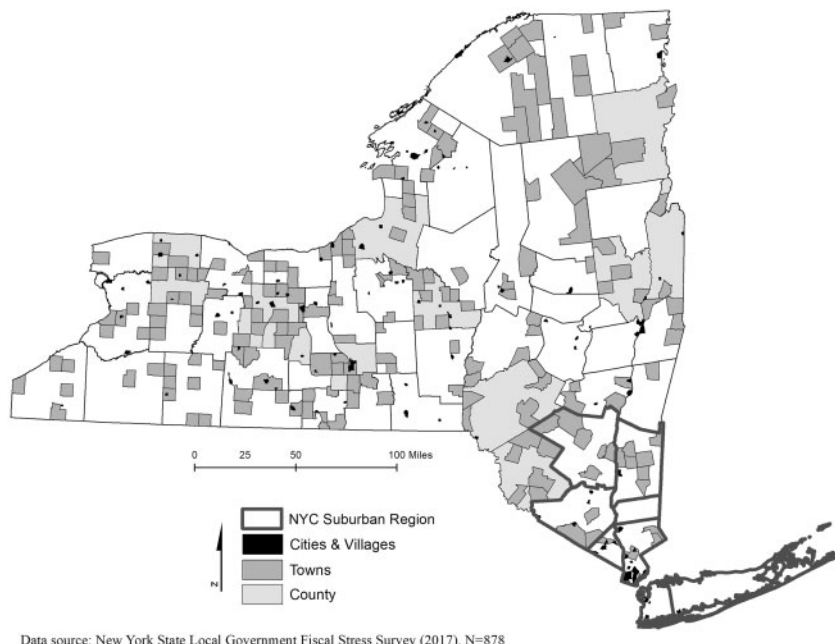
Our survey enables us to get beyond political ideology and assess the politics of state-local relationships within a federal system. The Governor of NYS promoted the passage of the tax cap with a narrative that blames local governments for being inefficient. While NYS is a high-tax/high-expenditure state, it also has the highest level of fiscal decentralization, meaning local governments shoulder more expenditure burdens compared to localities in other states (Xu and Warner 2016). Local governments can push back or acquiesce to state-level pressures (Warner and Clifton 2014). To capture push back on these pressures, our survey asked respondents their level of agreement for the following statement: “The governing board in my jurisdiction believes we should push back against the Governor’s narrative of local government inefficiency.” Responses followed a 5-point Likert scale of “strongly disagree” (1) to “strongly agree” (5), and the average response was 4.0 (“agree”). We expect localities that support pushback against the Governor’s narrative will be more likely to override.

On the other hand, localities may buy into the narrative of local government inefficiency. We asked survey respondents to indicate their level of agreement with the following statement on the same 5-point Likert scale: “The governing board in my jurisdiction believes the Governor’s narrative that New York’s property taxes are too high because of too many inefficient local governments.” The average was 1.8 (“disagree”), and we expect jurisdictions that agree more with this statement to be less likely to override as they view themselves as inefficient and overrides would not be fiscally responsible.

To increase the level of voter pressure on local government taxing decisions, the Governor implemented a Tax Freeze Rebate program that provided a state rebate on property taxes if the local government stayed under the tax cap and submitted a government efficiency plan to increase shared services (Aldag and Warner 2018). We include a dummy variable that indicates whether a government efficiency plan was submitted (submitted = 1; otherwise = 0; our survey). We expect local governments that submitted a government efficiency plan to be less likely to override the tax cap. Note that all three of these variables measure governing board attitudes toward political pressures coming from the Governor, which were designed to increase voter pressure from below, to encourage local governments to stay under the cap. We do not have measures of actual levels of local government efficiency.

### ***Demographic variables***

Previous research on TEL overrides by popular referenda identified demography as a key driver,<sup>3</sup> but no studies fully consider these drivers in predicting local legislative overrides. We include the following demographic variables: natural log of population, percent of population in poverty, percent of population with a college degree, and percent of population over age sixty-five. All demographic variables come from 2011 to 2015 ACS averages.



**Figure 1** Map of overrides of property tax cap, New York State local governments.

Finally, we account for geography. Recall that NYC is the only local government in NYS that is exempt from the tax cap. We hypothesize that localities within the suburban fringe of NYC are less likely to override the property tax cap when compared to Upstate jurisdictions, because they can freeride on services provided by the urban core. Fiscal equivalence is necessary for a decentralized system to deliver efficiency, but fragmentation can also lead to freeriding. Previous studies have found suburbs freeride on urban services (Homsy and Warner 2015; Kantor and Nelles 2015). To account for this in the model, we include a dummy variable for jurisdictions which are located within the Combined Statistical Area (CSA) of NYC (NYC suburban region = 1; otherwise = 0), as defined by the United States Office of Management and Budget (18.2 percent of the sample). Figure 1 shows a map of overriding jurisdictions in NYS and we see that overrides are higher outside the NYC suburban area.

## Results

We ran a logistic regression model that includes structural and local variables of fiscal stress, demographics, and political attitudes to assess how well fiscal federalism principles explain local governing board decisions to override a TEL. Table 3 shows the odds ratio and standard errors for our two models.<sup>4</sup> First is a

**Table 3.** Logistic model results: Local government likelihood to override the tax cap in New York State

	Structural model		Full model	
	Odds ratio	SE	Odds ratio	SE
<i>Structural variables</i>				
<i>Fiscal/economic</i>				
Comptroller fiscal stress rating <sup>a</sup>	1.019**	0.007	1.016*	0.008
Employee benefits as % expenditure <sup>b</sup>	1.036*	0.018	1.047*	0.020
Property tax dependence <sup>b</sup>	1.005	0.004	1.008	0.005
% Employment change <sup>c,d</sup>	0.949**	0.016	0.946**	0.018
<i>Demographic</i>				
ln (Population) <sup>c</sup>	0.957	0.074	0.919	0.081
Poverty (%) <sup>c</sup>	0.98	0.015	0.973	0.017
College educated (%) <sup>c</sup>	1.009	0.007	1.007	0.008
Above 65 (%) <sup>c</sup>	0.988	0.017	0.987	0.018
NYC suburban region (dummy, yes=1) <sup>c</sup>	0.481**	0.137	0.480*	0.146
<i>Local response variables</i>				
<i>Fiscal/service delivery</i>				
Local perceptions of fiscal stress <sup>e</sup>			1.298*	0.148
Tax exempt land contribution to fiscal stress <sup>b</sup>			1.458***	0.157
Property taxing effort <sup>b</sup>			0.541*	0.168
Cutback in road repair (dummy, yes=1) <sup>e</sup>			1.612*	0.330
Total services provided <sup>e</sup>			1.058*	0.028
<i>Political variables</i>				
Liberal governing board (dummy, yes=1) <sup>e</sup>			2.074	0.887
Pushback against Governor's narrative <sup>e</sup>			1.253**	0.101
Believe local inefficiency narrative <sup>e</sup>			0.841*	0.071
Submitted government efficiency plan (dummy, yes=1) <sup>e</sup>			0.422***	0.083
Constant	0.429	0.326	0.069	0.066
N		609		
Log likelihood	-390.78		-351.48	
Pseudo R <sup>2</sup>	3.2		12.94	

Notes: \* $P < 0.05$ ; \*\* $P < 0.01$ , \*\*\* $P < 0.001$ ;  $N = 609$ , New York State local governments.

Sources: <sup>a</sup>New York State Comptroller Fiscal Stress Monitoring System (2016); <sup>b</sup>New York State Comptroller Financial Data on Local Governments (2015); <sup>c</sup>American Community Survey 5-year estimates (2011–2015), <sup>d</sup>American Community Survey 5-year estimates (2005–2009); <sup>e</sup>New York State Local Government Fiscal Stress Survey (2017).

simple model of structural variables. It shows that localities with greater measures of structural fiscal stress (as measured by the Comptroller), greater employee benefits as a percent of total expenditure, and economic decline (as measured by negative changes in employment) are more likely to override. In contrast, places in the NYC suburban region are less likely to override (odds ratio = 0.481). These results are as hypothesized. The second is our full model, which includes the local variables provided by our statewide survey. We note that the explanatory value of the full model is four times greater than the explanatory value of the structural model (as measured by pseudo  $R^2$ ), and it allows us to test for fiscal federalism motivators.

In the full model, we find that the four structural drivers, significant in the structural model, remain significant. Places in the NYC suburban area are less likely to override, while fiscal stress (both the structural measure of fiscal stress and the broader measure based on local perception), employee benefits costs, and economic stress (as measured by employment decline) are linked to greater likelihood of overrides. We also find local officials' perceptions of the changing economy to be an important driver of overrides. Localities that identified tax-exempt land as a driver of their level of local fiscal stress are more likely to override the tax cap (odds ratio = 1.458), as expected. As fiscal federalism would predict, localities whose property taxing effort is higher are less likely to override the tax cap (odds ratio = 0.541). Meanwhile, property tax dependence has no effect on overrides, contrary to our expectations. Thus, we see that broader economic factors are primary drivers of the decision to override, and high tax effort causes local governments to be less likely to override. These results lend support to fiscal federalism notions of local government behavior and do not support the "Leviathan" notions of public choice.

We now turn to our political variables. First we see that political ideology of the governing board is not related to tax cap overrides. These results are in line with our expectation that fiscal responsibility is driving local governments' taxing decisions. Looking inside the politics of state-local relations, we find a more interesting story. If the governing board's attitude supported "push back against the Governor's narrative of local government inefficiency," then it was more likely to override the tax cap (odds ratio = 1.253). The opposite is true for governments which "believe the Governor's local government inefficiency narrative." Governments that buy into the narrative, on the same 5-point scale, are less likely to override the tax cap (odds ratio = 0.841). Similarly, if the local government submitted a government efficiency plan for its residents to qualify for the Tax Freeze Rebate program, a proxy for citizen pressure on local taxing decisions, it also was less likely (odds ratio = 0.422) to override the tax cap compared to jurisdictions that did not submit one. Believing the narrative of local government inefficiency and submitting a government efficiency plan signal

acquiescence to the state's political rhetoric and concern for citizen pressure on local taxing decisions. These lead to lower odds of override, suggesting that citizen pressures to control local government are effective.

Fiscal federalism argues that local governments primarily play a developmental role. Our results lend support to that claim. Places that made cuts in road repair, a key developmental expenditure, are more likely to override the tax cap (odds ratio = 1.612) when compared to localities that did not make these service cuts. Similarly, places that provide more services were more likely to override. Thus, we see that local governments experiencing service pressures may have to exceed the tax cap in order to fulfill their developmental role. However, poverty and elderly, two of our demographic controls that measure need for redistributive expenditures, have no significant effect on overrides. Thus, in keeping with fiscal federalism expectations, we find that it is the developmental and *not* the redistributive role of local governments that drives overrides.

In contrast to other TEL override studies, which find demographic controls are significant drivers of public referenda-based overrides, none of these were significant in explaining local legislative overrides in our model. Our results suggest the taxing behavior of voters and local governing boards are different, and fiscal federalism factors are primary drivers of legislative overrides of TELs.

## Discussion

What drives local government taxation behavior? We use a recently implemented levy limit in NYS that allows local legislative overrides to answer this question. Proponents of state-imposed TELs on local governments argue that local governments have a Leviathan tendency that can only be controlled with a legislative cap on tax increases. In contrast, fiscal federalism argues that efficiency and effectiveness can be achieved in a decentralized system of governments with higher levels of government providing redistributive services; and lower levels of government promoting development (Musgrave 1959, Peterson 1981) and competing to provide the best tax-services bundle (Oates 1972; Tiebout 1956). We find only limited support for a local Leviathan driving levy limit overrides, and stronger support for fiscally responsible behavior that aligns with the promises of fiscal federalism that local governments are pragmatic managers (Kim and Warner 2016).

Legislative overrides are linked to the need to provide more services and developmental spending. We see a greater likelihood of overrides in local governments that cut back on road repair and those with employment decline. Xu and Warner (2016) warned fiscal stress may be crowding out developmental expenditures at the local level. Our results suggest that NYS local governments are trying to fulfill their developmental responsibilities, and overrides reflect their effort

to do so. Although overriding the tax cap in NYS is easy in theory, the political costs are still high in the post-Great Recession context of anti-tax sentiments. The Governor's Tax Freeze Rebate program capitalized on these anti-tax sentiments. It might be easier politically to stay under the tax cap, but in places with higher fiscal stress, we find local officials are willing to risk the loss in voter support and pragmatically push back on state level TEL policy to exercise fiscal responsibility.

Structural conditions and development needs drive local governments' decisions to override the tax cap, but local governments are also keenly aware of the tax burden on residents. Fiscal federalism's principle of providing the best tax-service combination seems to be at work, rather than a budget-maximizing behavior. Localities with higher tax effort are less likely to override the tax cap, while places that report weaker tax bases due to tax exempt land are more likely to override the tax cap.

Under fiscal federalism, local government decisions are checked by voter pressures from below and state pressures from above. State legislation dictates most employee benefit costs in NYS, and this non-negotiable expenditure item is linked to a higher likelihood of overrides (benefit expenditures are not exempt from the tax cap).

One contribution of our study is the different findings from previous studies of TEL overrides via public referendum. While the TEL in NYS is unique in that the override decision is in the hands of the local governing board, most TELs put this decision in the hands of voters (via a referendum). The assumption, following "Leviathan" public choice notions, is that voters will exercise more fiscal responsibility than local officials. However, earlier studies on TEL overrides via referendum found overrides are less common in jurisdictions which are poorer, less educated, and have lower property tax dependence (Lowery and Sigelman 1981; Ladd 1978; Ladd and Wilson 1983). In short, where service needs are higher, voters are less likely to allow local governments to collect the necessary revenues. This can lead to increasing inequality in service levels across jurisdictions. In contrast, we find that when the override decision is up to local governing boards, their decisions are more pragmatic and balance developmental needs (but not redistributive needs, which are primarily the purview of state government) with the desire to keep taxes low.

We find fiscal federalism still holds, with local governments pursuing development and striving to provide the best tax-service combination. However, a caveat of our findings is we are studying the early impacts of a relatively flexible TEL. As the impacts of TELs deepen over time (Mullins 2004; Rivera and Xu 2014), it may become more difficult for poorer jurisdictions to override. In the future, TELs may undermine fiscal federalism's ability to deliver efficiency and effectiveness at the local level.



**Table 4.** Regional differences between upstate and NYC suburban local governments

	Group mean		P-value
	Upstate (N = 498)	NYC suburban region (N = 111)	
<i>Structural variables</i>			
<i>Fiscal/economic</i>			
Comptroller fiscal stress rating <sup>a</sup>	11.700	12.300	0.598
Employee benefits as % expenditure <sup>b</sup>	13.700	17.300	0.000
Property tax dependence <sup>4b</sup>	48.100	63.600	0.000
% Employment change <sup>c,d</sup>	-0.630	-0.090	0.273
<i>Demographic</i>			
ln (Population) <sup>c</sup>	8.010	8.720	0.000
Poverty (%) <sup>c</sup>	13.500	7.500	0.000
College educated (%) <sup>c</sup>	23.400	46.600	0.000
Above 65 (%) <sup>c</sup>	17.000	17.800	0.122
<i>Local response variables</i>			
<i>Fiscal/service delivery</i>			
Local perceptions of fiscal stress <sup>e</sup>	2.4	2.1	0.005
Tax exempt land contribution to fiscal stress <sup>b</sup>	2.7	2.6	0.105
Property taxing effort <sup>b</sup>	0.61	0.54	0.017
Cutback in road repair (dummy, yes=1) <sup>e</sup>	0.29	0.26	0.550
Total services provided <sup>c</sup>	8.05	8.58	0.192
<i>Political variables</i>			
Liberal governing board (dummy, yes=1) <sup>e</sup>	0.04	0.08	0.038
Pushback against Governor's narrative <sup>e</sup>	4.02	3.83	0.091
Believe local inefficiency narrative <sup>e</sup>	1.8	1.73	0.487
Submitted government efficiency plan (dummy, yes=1) <sup>e</sup>	0.59	0.67	0.070

Notes: P-values derived from two tailed t-test of means between upstate and localities within the NYC suburban region. N = 609, New York State local governments.

Sources: <sup>a</sup>New York State Comptroller Fiscal Stress Monitoring System (2016); <sup>b</sup>New York State Comptroller Financial Data on Local Governments (2015); <sup>c</sup>American Community Survey 5-year estimates (2011–2015); <sup>d</sup>American Community Survey 5-year estimates (2005–2009); <sup>e</sup>New York State Local Government Fiscal Stress Survey (2017).

Our results also highlight an unresolved task for fiscal federalism: equity. Fiscal federalism argues decentralization allows governments to meet diverse local needs and preferences. However, a uniform state policy has different impacts on different communities. These differences are clear between the NYC suburban fringe and Upstate New York (table 4). Upstate jurisdictions, when compared to jurisdictions

in the NYC suburbs, indicate more self-assessed levels of fiscal stress, have lower rates of property tax dependence, and higher property taxing effort (because assessed values are lower in Upstate<sup>5</sup>). Demographically, Upstate municipalities are smaller, have more poverty, and lower education levels. Overrides are more prevalent among Upstate jurisdictions. By contrast, in the NYC suburban region the rate of overrides is lower. These jurisdictions have more property tax dependence and have not diversified their tax bases as much as Upstate. It is also possible that these suburban jurisdictions may not need to override because their residents can freeride on services from New York City, which is exempt from the tax cap. This would suggest that fiscal federalism does not deliver on its promise of fiscal equivalence, but that is a subject beyond the scope of our current research.

## Conclusion

We analyzed local government overrides of a new and relatively flexible levy limit in NYS to understand taxation behaviors of local governing boards. Our results suggest the warnings of Leviathan behaviors at the local level (e.g., [Brennan and Buchanan 1979](#); [Qian and Roland 1998](#); [Kornai 1986](#)) are overemphasized. Our study finds most local governments stayed under the tax cap and that local legislative overrides of state-imposed budget constraints are driven by local fiscal stress, and local governments' desire to fulfill their developmental role.

Local governments in NYS appear to be acting as good public stewards, even without the additional voter oversight of a public referendum requirement for levy increases. In fact, comparing our findings to studies of TEL overrides via public referendum (e.g., [Maher et al. 2017](#); [Roscoe 2014](#)) suggests local governing boards may be more fiscally responsible than voters. Thus, we return to the question, are TELs necessary to control local government budgets? We argue the dynamic economic, fiscal, and political pressures of fiscal federalism are controlling local budgets. Our results also raise concern that the additional rigidity from TELs may threaten local governments' ability to make tax and spending decisions in line with efficiency and effectiveness.

For fiscal federalism to work, local governments need to have the fiscal and political authority to fulfill their developmental role, work within fiscal equivalence, and compete with other localities to achieve efficiencies. State-imposed budget constraints, such as TELs, undercut these foundations by eroding local governments' ability to respond to local needs. Do states really need TELs to control local government spending? Our analysis suggests that TELs may undermine the principles of fiscal federalism and with them, local government efficiency and effectiveness, especially for local governments with the greatest developmental needs.

## Notes

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1. We lose 310 cases in our final analysis due to non-responses to survey questions. We ran models ( $N = 710$ ) excluding the variable that had the lowest response rate (local fiscal stress perception) and did not find significantly different results. We also conducted  $t$ -tests to check for non-response bias. The  $t$ -test results for population, property tax dependence, and taxing effort show no statistically significant differences between local governments that responded to our survey and those that did not.
2. Average employer contributions for police and fire pension plans as a percent of payroll increased from 15.1 percent in 2010 to 24.3 percent in 2017, and for all other local government employee pension plans contributions increased from 7.4 percent in 2010 to 15.5 percent in 2017 (Office of the New York State Comptroller 2010, 2017). These rates are determined by the State.
3. The following demographic variables have been shown to be important in voter support of TELs and local override measures: population (Maher et al. 2017), poverty (Roscoe 2014), education (Ladd and Wilson 1983; Lowery and Sigelman 1981; Roscoe 2014), and elderly (Lowery and Sigelman 1981).
4. We also ran models controlling for government type (county, city, town, and village) but did not find significant differences in our overall results and none of the government type variables were significant.
5. The five-year average full value (based on annual assessment rolls) for Upstate municipalities is \$150 million, and over \$175 million for municipalities located in the NYC suburban region (Office of the New York State Comptroller 2015).

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