

You Had Two Jobs

I've long been critical of local government. Yes, local officials are "closer to the people." And yes, moving to a new town is a lot cheaper than moving to a new state or a new country. Yet local governments are still far inferior to for-profit businesses.

Recently, however, I've realized that I've been too generous. The two main things that local governments do are:

1. Provide K-12 education.
2. Regulate construction.

And on reflection, local governments do *both* of these things terribly. Consider:

1. Voucher systems are clearly more efficient, yet virtually every locality continues to directly supply K-12 education. Nor is this a product of rising state and federal involvement. America's local governments have been funding systems, not students, for *centuries*.
2. Local governments' construction regulations are usually quite strict, especially in the most desirable locations. The resulting draconian system of height limits, zoning, minimum lot sizes, minimum parking requirements, and beyond roughly double the cost of housing and greatly retard national economic growth. While state and federal governments also regulate construction, local regulations are clearly vastly more important. That's why we call them Not In My Backyard policies.

Some economists try to rationalize the status quo, but to no avail.

1. While voucher systems' effect on test scores is debatable, the effect on *customer satisfaction* is not. How so? Because if you let parents take their money elsewhere, plenty will. Hence, they are not currently satisfied customers. You can deny that customer satisfaction is a good benchmark, but that's the standard we use for almost every other business. Why should education be any different?
2. While you can argue that housing regulations curtail negative externalities, the leading examples are parking and traffic. The optimal response to both is not construction regs, but peakload pricing. In any case, the damage of housing regulation vastly outweighs the harm of any negative externalities that it plausibly prevents. And what about all the positive externalities of construction? More homes means more playmates for my kids.

The other route is to concede the inefficiencies, but insist that local government still

“works.” After all, local governments are supposed to maximize the interests of their own citizens. And that’s what they do, right?

At least for housing regulation, this is superficially plausible. “Existing property owners benefit if you restrict supply to keep housing prices high” sounds right. Yet on reflection, this slogan is far less clear than it sounds. Most obviously, if housing prices in your region are high, and all of the *other* localities strictly regulate housing, deregulation allows *your* locality to sell out to developers and earn massive profits. Local deregulation is like violating your OPEC quota: In the absence of strident retaliation, it’s practically a license to print money.

How, though, can local government be so dysfunctional?

First, as I’ve argued before, non-profit competition is weaker than for-profit competition, even if the number of competitors is vast. Why? Because no one is trying very hard to win. As I’ve explained before:

Tiebout implicitly assumes that non-profit competition works the same way as for-profit competition. It doesn’t. If a business owner figures out how to produce the same good at a lower cost, he pockets all of the savings. If the CEO of a publicly-held corporation figures out how to produce the same good at a lower cost, he pockets a lot of the savings. But if the mayor of a city figures out how to deliver the same government services for lower taxes, he pockets none of the savings. That’s how non-profits “work.”

With non-profit incentives, neither the number of local governments nor the ease of exit lead to anything resembling perfectly competitive results. The “competitors” simply have little incentive to do a good job, so they all tend to perform poorly.

Second, voters are deeply irrational, even at the local level. Most people childishly refuse to grant that allowing more construction will reliably make housing more affordable.

Yes, you can point to my *Myth of the Rational Voter* and object, “How can voters be so irrational even though the expected cost of voter irrationality is especially high at the local level?” Reply: Even at the local level, the probability of voter decisiveness is so low that the expected cost of voter irrationality is approximately zero. If you have more than a

hundred voters, "Your vote doesn't count" is basically correct.

To reiterate, I am not arguing that local governments have two little blind spots. I am arguing that local governments have two main jobs – and they're awful at both.