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Voting suffrage and the political budget cycle: Evidence from the London Metropolitan Boroughs 1902–1937

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ABSTRACT

We study the opportunistic political budget cycle in the London Metropolitan Boroughs between 1902 and 1937 under two different suffrage regimes: taxpayer suffrage (1902–1914) and universal suffrage (1921–1937). We argue and find supporting evidence that the political budget cycle operates differently under the two types of suffrage. Taxpayer suffrage, where the right to vote and the obligation to pay local taxes are linked, encourages demands for retrenchment and the political budget cycle manifests itself in election year tax cuts and savings on administration costs. Universal suffrage, where all adult residents can vote irrespective of their taxpayer status, creates demands for productive public services and the political budget cycle manifests itself in election year hikes in capital spending and a reduction in current spending.

1. Introduction

Suffrage rules regulate who can vote and this, in turn, influences the interests served by elected politicians. While today we associate democracy with equal and universal suffrage, historically the power to elect or appoint representatives was the privilege of narrow elites. Suffrage rules focussed on specific characteristics of the individual such as ownership of property, payment of taxes, residency and gender. The logic behind linking the right to vote to property holdings or tax payments can be traced back to mediaeval Britain and reflected the belief that it restricted the franchise to individuals with a longer-term interest in the welfare of the community, akin to the shareholders of corporations.

Economic models in the tradition of Meltzer and Richard (1981) predict a straightforward positive link between demands for public goods and redistribution and extension of the franchise. However, evidence from analyses of historical data show that the impacts were more complex than predicted by theory and were functions of the specific rules that determined who could vote.[2] While progress has been made in understanding the public finance consequences of franchise extension, little is known about the influence these rules have on the incentive to manipulate tax and spending patterns prior to elections in the quest for votes. A well-established literature, drawing on evidence from modern democracies and surveyed by Paldam (1997), Alesina et al. (1997) and most recently by Drazen (2008), offers a strong argument for the existence of opportunistic political budget cycles in both national and local elections.[3] The construction of cross-country datasets

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[2] See, e.g., Aidt and Jensen (2009) for evidence that the likelihood of (progressive) income tax during the long 19th century is reduced by suffrage reform; and Kenny and Winer (2006) for evidence from the post-war period that greater political freedom does not necessarily lead to more redistribution. Aidt et al. (2010) show that franchise reform can lead to a reduction in spending. See also Lindert (1994, 2004a,b), Husted and Kenny (1997), Aidt et al. (2006), Aidt and Eterovic (2011), Aidt and Jensen (2013), and Engerman and Sokoloff (2011).

[3] See, for example, Paldam (1979), Roubini and Sachs (1989), Alesina et al. (1992), Blais and Nadeau (1992), Rosenberg (1992), Schuknecht (1996), Franzese (2000), Seitz (2000), Kneebone and McKenzie (2001), Galli and Rossi (2002), Akhmedov and Zhuravskaya (2004), Andrikopoulos et al. (2004), Shi and Svensson (2006), Veiga and Veiga (2007), Baleiras and Costa (2004), Mink and de Haan (2006), Foucault et al. (2008), Brender and Drazen (2008), Vergne (2009), Drazen and Eslava (2010), Potrafke (2010, 2012), Efthyvoulou (2011), Sakurai and Menezes-Filho (2011), Aidt et al. (2011), and Klomp and De Haan (2013b). The literature was initiated by the classical papers by Nordhaus (1975) and Rogoff and Sibert (1988).

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(of OECD countries and more recently of developing countries) and of rich datasets for local governments (municipalities or states) from the modern period has tended to draw attention to the experience of the late 20th and early 21st centuries at the expense of earlier periods. Consequently the focus has been on opportunistic political budget cycles operating under universal suffrage; quite how the cycle might manifest itself in polities with economic and social restrictions on who could vote has been completely overlooked.

The purpose of this paper is to draw upon the historical experience of early 20th century London to study the nature of the political budget cycle under two different suffrage regimes: taxpayer suffrage, where the right to vote is linked to specific tax payments; and universal suffrage, where all adults can vote (with minor qualifications), irrespective of their economic status. While the identity of the "pivotal voter" differs systematically under the two suffrage rules, electorally-motivated politicians can be expected to be equally determined to manipulate fiscal policy before elections to win support from the pivotal voter. We, therefore, conjecture that an opportunistic political budget cycle will be present in both regimes but that its nature will vary systematically with the suffrage rules.[4]

The setting for our study is the London Metropolitan Boroughs (LMBs) before and after the First World War. The 28 LMBs were established in 1899 and had powers to levy local property taxes, to decide on the provision of local services (sewer connections, bathhouses, parks, libraries, dairies and milk shops, etc.) and to take out loans to finance capital expenses on the security of future property taxes. Within the statutory boundaries, the LMBs had significant fiscal autonomy and the elected representatives of the councils could decide on the level, composition and the timing of key fiscal variables. All councillors were elected every three years. The franchise before the First World War was based on property tax payment and restricted to men; we refer to it as taxpayer suffrage. The Representation of the People Act (sometimes referred to as the Fourth Reform Act) in 1918 eradicated the tax payment requirement at all levels of government (including for the LMBs) and introduced almost equal and universal suffrage.[5] This quasi-natural experiment allows us to study the opportunistic political budget cycle under two different suffrage regimes.[6]

Besides adding new historical evidence to the debate on the opportunistic political budget cycle, our study contributes directly to two more specific strands of literature.[7] Firstly, it significantly enhances our understanding of fiscal retrenchment and taxpayer democracy in Britain. Until 1918, voting rights in local elections linked representation to the prompt payment of the local property tax (known in Britain as the rate) such that only local taxpayers had the right to vote. This had intriguing implications for the relationship between the size of the electorate and local public finance. In particular when the balance of power shifted to small-scale, middle class taxpayer-voters, demands were made for retrenchment and economy rather than fiscal expansion, despite apparently large social returns on public investment in local public goods (Hennock, 1963, 1973; Wohl, 1983; Szreter, 1988, 1997). As documented by Aidt et al. (2010), this generated a negative relationship between spending on local public goods and the extension of the franchise.[8] We add to this by studying how opportunistic political budget cycles operate in an environment with taxpayer-voters. This restricted franchise is compared to the regime of universal suffrage, where the pivotal voter often does not contribute much to the local tax base.

Secondly, our study contributes to the fast expanding research on the *conditional* political budget cycle initiated by Persson and Tabellini (2003), Brender and Drazen (2005), Shi and Svensson (2006), Alt and Lassen (2006a,b) and Alt and Rose (2007) amongst others, and recently surveyed by de Haan and Klomp (2013). The general point here is that the size and nature of the political budget cycle are conditional on the political and economic environment. They depend, amongst other factors, on economic conditions (e.g., the level of income), the institutional framework (e.g., the level of corruption, the type of election or political system), and the monitoring framework (e.g., fiscal transparency and quality of the press). We add an important dimension to this conditionality by showing that the opportunistic political budget cycle is influenced by the details of the franchise.

We find the following results. Under taxpayer suffrage (1902–1914), the opportunistic political budget cycle materializes as tax cuts and in reduced spending on administration in election years. Under universal suffrage (1921–1937), we find that expenditures in election years are shifted towards productive public goods (capital spending) and away from other types of (current) spending, with no effect on tax income. The LMBs operated under a balanced budget rule which limited their ability to deficit finance election year tax cuts or spending booms, yet we find evidence of smaller surpluses in election years under both suffrage regimes.

We interpret these findings in the light of the different incentives that variations in the suffrage rules generate for politicians to engineer opportunistic cycles. Building on Lohmann (1998), Shi and Svensson (2006), and Aidt et al. (2010), we provide a formal rational choice model that illustrates the logic. Under a restricted taxpayer suffrage that explicitly disenfranchises non-taxpayers and enfranchises owners of property in the locality who can reside elsewhere, taxpayer-voters often demand retrenchment and economy. Politicians respond to this by cutting taxes and reducing spending on administration in election years, as we observe in the data. In contrast, under universal suffrage all adult residents hold the right to vote, including many poorer residents who contribute little in terms of property tax payments to the funding of spending. This generates demand for fiscal expansion. Politicians, therefore, aim to engineer additional electoral support by adjusting the portfolio of spending towards productive public services which benefit the pivotal voter and away from other spending without necessarily increasing taxes.

The rest of the paper is organized as follows. In Section 2, we introduce the institutional setting of our study and the particularities of the suffrage rules governing elections to the councils of the LMBs before and after the First World War. In Section 3, we develop the theoretical foundation for our empirical investigation. To this end, we sketch a rational choice model and provide an online supplementary appendix with technical details. In Section 4, we present the data and discuss some stylized facts about local public finance in London between 1902 and 1937. In Section 5, we consider the evidence of an opportunistic political budget cycle. In Section 6, we lay out our empirical strategy. We present the main findings in Section 7 and in Section 8 we discuss alternative interpretations and robustness checks. The concluding remarks in Section 9 recapitulate our findings in the context of conditional political budget cycles.

[4] While the franchise rules may also affect the nature of party politics, we do not expect systematically different partisan cycles (budget cycles which are driven by differences in the ideological preposition of the majority party) under the two regimes. We use a robustness check to test the validity of this assumption.

[5] The suffrage was neither equal (in that, for example, graduates of certain universities could vote twice) nor universal (in that it excluded unmarried and younger women who had to wait until 1928 to get the vote).

[6] Klomp and De Haan (2013a) have recently challenged whether it is appropriate to restrict the coefficient on the election cycle indicator to be homogenous across countries. As with other studies that make use of local government data, e.g., Veiga and Veiga (2007), our study is less open to this critique because the institutional and economic environment is broadly the same across the LMBs.

[7] Heckelman and Whaples (1996) is the only other study we are aware of which investigates the political business cycle (in GDP in the USA) from a historical perspective.

[8] For a discussion of under-investment in the urban amenities and infrastructure during the 19th century, see Williamson (1990). The life expectancy data reported in Szreter and Mooney (1998) demonstrate that the situation did not improve much until late in the century.