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Judicial independence and economic freedom in the US states

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ABSTRACT

This article addresses the extent to which differences in judicial independence across US states influence economic freedom by using the Fraser Institute's Economic Freedom of North America Index. Overall, the results suggest that, as judicial independence increases within a state's court of last resort, so does a state's overall economic freedom score, along with each of the sub-component index scores. These findings add important nuances to the literature and provide opportunities for future research.

KEYWORDS

Judicial independence; economic freedom; credible commitments; judicial selection

JEL CLASSIFICATION

D72; H73; O49

I. Introduction

There has been a significant body of research evaluating judicial independence (JI) and how this impacts a number of economic outcomes. This work is largely concerned with the extent to which the rule of law exists within a region and how this ties to economic freedom and economic growth (see broadly North 1990; Glaeser et al. 2004; and for an extensive review of the literature, Berggren 2003). Here, when the rule of law is functioning, it provides the incentives necessary for entrepreneurs to pursue productive activities that then lead to economic growth and development.

Though this area has seen increased interest by academics across disciplines, less has been done to evaluate how JI influences and impacts economic freedom. This article adds to that literature by empirically investigating how JI may, if at all, enhance economic freedom within the 50 US states. The literature has shown a causal link between JI and economic growth, as increased JI creates greater long-run stability and enhances the rule of law by providing an independent, third-party arbitrator when disputes arise between both private individuals and public officials (Feld and Voigt 2003; Glaeser et al. 2004). This mechanism should increase economic freedoms by ensuring that all disputes are resolved in an impartial manner and that other branches of government do not act in an arbitrary

or confiscatory way. Thus, greater JI provides relatively more predictability and consistency in the application of the law and, thereby, enhances economic freedoms and increases economic growth.

This study adds to several strands of the literature, one of which is the extent to which JI might expand and increase economic freedoms. Overall, there is a strong connection between increased JI, rule of law, the protection of private property, economic freedom and economic growth (Torstensson 1994; Barro 1997; Hall and Jones 1999; Olson, Sarna, and Swamy 2000; Feld and Voigt 2003). Several other important studies have specifically found a causal link, when making international comparisons, between improved JI and increased economic freedom (Glaeser et al. 2004).

The current article contributes to the above literature in several important ways. First, it addresses how, if at all, JI impacts economic freedoms across the US states. This is important as, to the best of the author's knowledge, no other study has systematically considered this connection across states. However, research has shown that there does exist significant differences in JI (Berkowitz and Clay 2006; Dove 2015; Hanssen 2004). The analysis also ensures that a number of social norms and other unobserved variables are automatically controlled for that are much more difficult to account for in international studies.

Finally, evaluating the US states allows for the exploitation of a readymade dataset in the Economic Freedom of North America (EFNA) index, compiled by the Fraser Institute, which measures both overall economic freedom across states as well as several subcomponents of economic freedom, including ‘size of government’, ‘taxation and discriminatory takings’ and ‘labour market freedoms’.¹ This dataset helps avoid the need for survey data or other subjective determinations of what constitutes economic freedom while also pinpointing specific aspects of economic freedom that are most likely influenced by JI.

The remainder of the article is structured as follows: Section II considers some brief theoretical justifications for why it is that a relatively independent judiciary might lead to increased economic freedom along with a discussion of the data employed. Section III lists and discusses the results, while Section IV concludes.

II. Theory and data description

The importance that JI plays in increasing economic freedom lies in the fact that it creates an independent and unbiased third-party arbitrator to resolve disputes. This fosters the opportunities for private individuals to more effectively pursue long-term plans and investment (Feld and Voigt 2003). JI also conveys a credible commitment by the state to economic actors (North and Weingast 1989), which renders property rights more secure and ensures that public predation is minimized or, at least, carried out in a procedurally consistent fashion. This further increases the opportunities for individuals to pursue productive economic activity.

Thus, not only should greater JI enhance overall economic freedom, it should also hold that both the ‘size of government’ and ‘taxation and discriminatory takings’ subcomponents will outperform, relative to states with less JI. These findings have been suggested by Kantorowicz (2014) and Tridmas (2005). Further, if relatively more JI is able to impartially resolve contract disputes between private

citizens, then ‘labour market freedom’ should perform better in those states with greater JI as well. This has also been suggested by Besley and Payne (2003), who find evidence that there are significantly more employment discrimination lawsuits in states that elect judges along partisan lines.

In order to empirically evaluate JI, the current article follows what has effectively become convention within the literature,² and includes measures for the method of selection and retention of judges, salaries in real 2012 dollars, tenure in years and independent oversight – all within state courts of last resort.³ The article includes two variables for judicial selection, which is whether a state selects judges through merit selection (considered the most independent) and appointment or nonpartisan elections, which are considered less independent than merit selection but more so than partisan elections.⁴ The next two variables are whether judges are retained to the bench through unopposed popular retention elections or are reappointed by some other branch of government.

The next two variables include judicial salaries and term lengths, both of which are considered to increase judicial independence as they both increase (Cordis 2009). Finally, two additional dummy variables represent whether states also employ judicial nominating and judicial retention commissions. Both are nonpartisan bodies, where the former is tasked with providing potential candidates to a governor or legislature for selection, while the latter provides information to voters about a given candidate. Each increases checks and balances in the selection process and, thus, increases JI.

In order to operationalize those measures, the article constructs a single measure of JI through principal component analysis. The first principal component is taken from each of the variables discussed above in order to create an overall index. This index is then normalized to range between 0 and 10, with 0 representing extremely low levels and 10 representing extremely high levels of JI. This JI index is then used to evaluate its influence on economic freedom, drawn from the EFNA index. Each

¹Information on the indices as well as datasets are freely available at: www.freetheworld.com/efna.html

²See Hanssen (2004), Feld and Voigt (2003), and Dove (2015) for relevant overviews of this literature.

³Data on judicial salaries come from The National Center for State Courts and are freely available at www.ncsc.org

⁴Merit selection developed as a means to better insulate the judiciary from external bias and influence (Hanssen 2004). Usually, under this method, an independent commission provides candidates for selection by other branches of government. These individuals will then periodically face unopposed retention elections by the electorate, who are required to decide whether the given judge should remain on the bench.

category of the EFNA runs from '0' (no economic freedom) to '10' (most economic freedom). Importantly, this is not an absolute scale, but rather, a relative scale. Therefore, the values show the level of economic freedom in one state relative to other states. These data run from 1981 through 2011, which, for the purposes of this article, are averaged over those years.⁵

III. Results and interpretation

The crux of the empirical analysis can be found in the relationships shown in Figs 1 and 2. Each figure provides the effect that JI has on the overall EFNA score (top-left panel), the 'size of government' component (top-right panel), the 'taxation and discriminatory takings panel' (bottom left) and 'labour market freedom' (bottom right), each broken down into quintiles for Fig. 1 and by individual states in Fig. 2.

There is clearly an upward trend for each of the components of the EFNA, suggesting that, as JI increases within states, so too does economic freedom. This would appear to be especially true for the

first and second quintiles in Fig. 1 and each of the trends in Fig. 2.

As an additional specification, I include several cross-sectional OLS regressions. These regressions include a number of control variables common to the literature. The controls are the percentage of the population with a bachelor's degree or higher, median age, the percentage of the population that is male and the percentage of the population that is white. Again, each of these variables are averaged over the sample period 1981–2011, except for the education variable, which is averaged from 1989 to 2009.⁶ Finally, I include a set of regional dummy variables based on each of the US Census regions for the northeast, mid-west, west, and south, as Berkowitz and Clay (2006) suggest that colonial origin of a state plays a significant role in a state's current level of JI. Table 1 provides the regression results.

It should be noted that, given the construction of the index, it is not possible to interpret the actual coefficient; however, what is important for the analysis is the actual sign and significance of the coefficient obtained for the JI index score. Columns 1 through 3 present the results when the overall

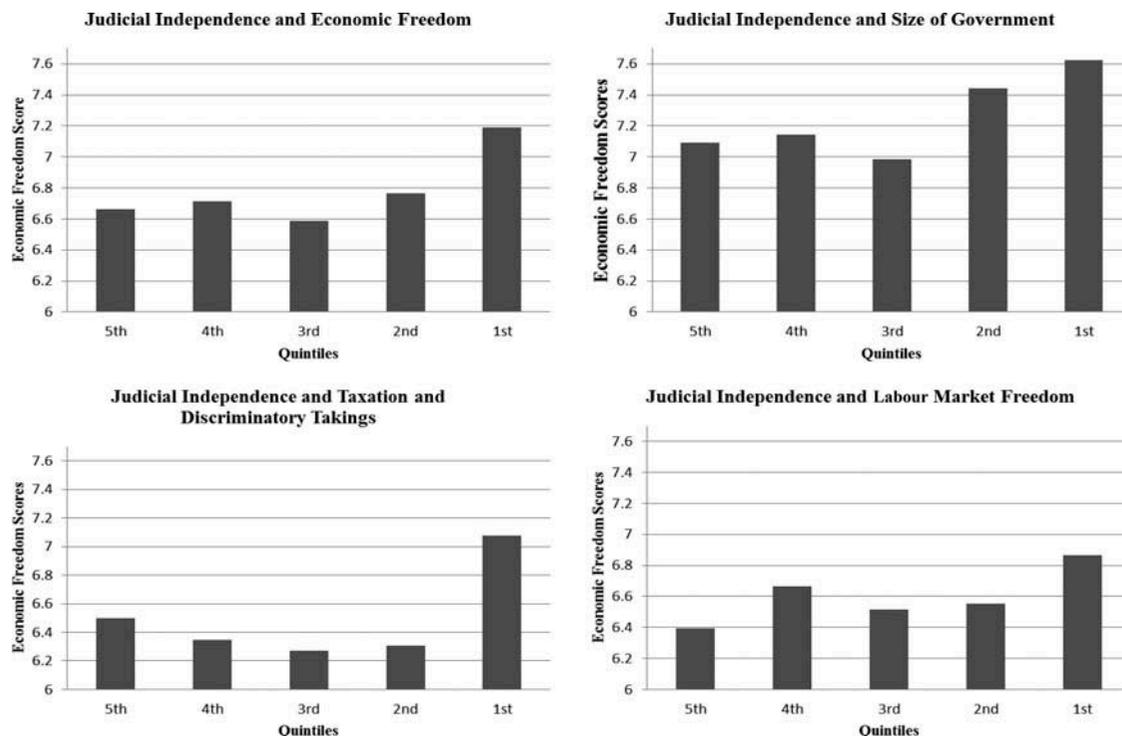


Figure 1. Relationship between judicial independence and economic freedom by quintile.

⁵This is done as there was little to no variation in the JI variables, meaning that panel data are not amenable to analysis.

⁶Data for all control variables were taken from the US Census. Data are freely available at: www.census.gov

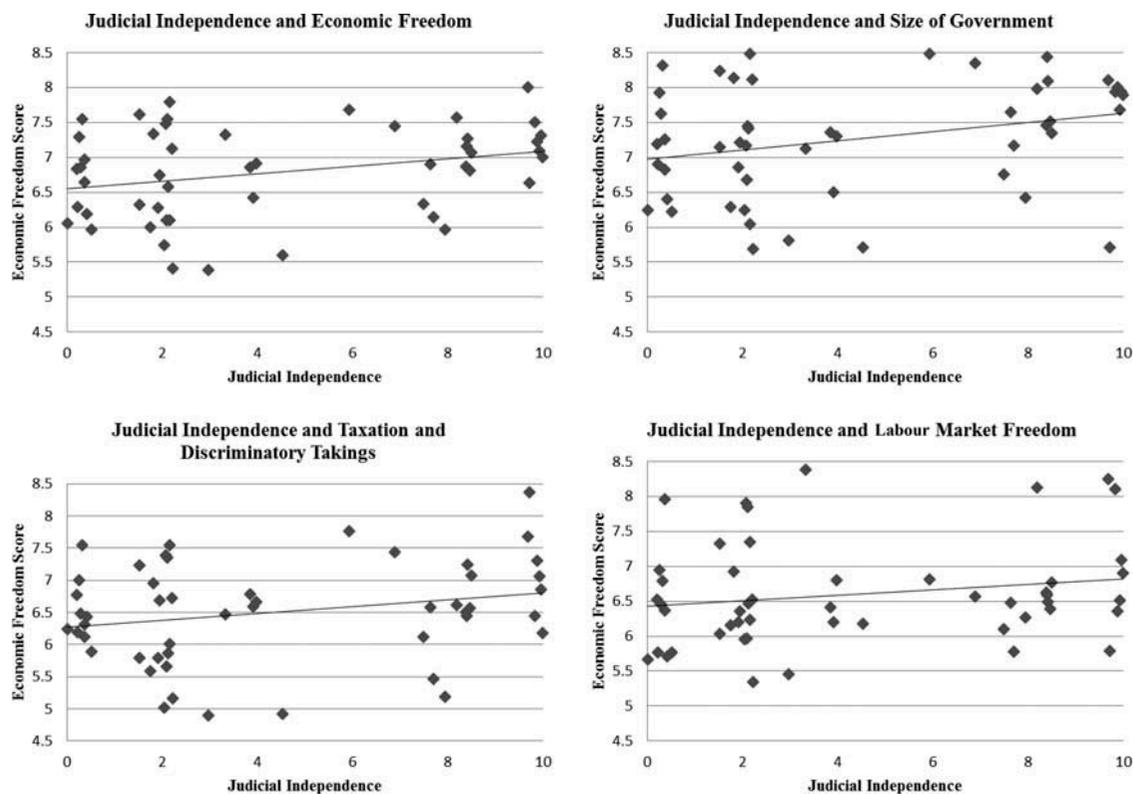


Figure 2. Relationship between judicial independence and economic freedom by state.

economic freedom score is employed as the dependent variable, columns 4 through 6 with 'size of government', columns 7 through 9 incorporate 'taxation and discriminatory takings', while columns 10 through 12 use 'labour market freedom'. Further, column 1 does not include any controls; column 2 includes all socioeconomic control variables, but excludes the regional dummy variables while column 3 includes all control variables. Columns 4 through 12 follow the same format.

Overall, every result suggests that as JI increases, so too does each of the components of economic freedom. Further, there appears to be a highly statistically significant relationship between JI and overall economic freedom along with the 'size of government' variable in every specification. Interestingly, although the sign coefficients are positive when analysing the 'taxation and discriminatory takings' and 'labour market freedom' measures, only columns 7 and 12 for each, respectively, are statistically significant. Thus, the findings suggest that the impact that JI has on these latter two subcomponents of economic freedom are much less robust as compared to overall economic freedom and 'size of government'.

These results do conform to some of the findings within international studies, with the evidence suggesting that, even across US states, greater JI also has a profound and significant effect on various aspects of economic freedom, including both overall economic freedom and also the 'size of government' as measured by the EFNA. Although less robust, the results also suggest that greater JI does improve the 'taxation and discriminatory takings' and 'labour market freedom' scores as well. These findings should provide ample opportunities for future research and should help shed light on the exact channels through which JI secures and increases economic freedoms available to economic agents.

IV. Conclusion

This article has compared JI as it exists across the US states on a number of margins in order to evaluate its effect on economic freedom as measured by the EFNA Index compiled by the Fraser Institute. The results suggest that relatively more JI increases economic freedom – both overall and for several of the subcategories that comprise the EFNA Index. This article has added important new insights about the

Table 1. OLS regression results for judicial independence and economic freedom.

VARIABLES	Independent variable = average overall economic freedom score and subcomponent scores from 1981 to 2011											
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Judicial independence index score	0.0531** (0.0213)	0.0509** (0.0242)	0.0577** (0.0226)	0.0655** (0.0293)	0.0622** (0.0287)	0.0639** (0.0276)	0.0535* (0.0281)	0.0413 (0.0301)	0.0451 (0.0278)	0.0392 (0.0298)	0.0484 (0.0299)	0.0571* (0.0284)
Average per cent bachelor degree or higher		0.00514 (0.0295)	0.0228 (0.0269)		0.0308 (0.0365)	0.0488 (0.0359)		-0.0111 (0.0348)	0.00505 (0.0312)		-0.00554 (0.0265)	0.0133 (0.0252)
Average age		-0.116 (0.0708)	-0.114* (0.0628)		-0.0999 (0.0691)	-0.100 (0.0604)		-0.137* (0.0798)	-0.151** (0.0674)		-0.112 (0.0845)	-0.0915 (0.0844)
Average per cent male		-0.258** (0.118)	-0.0787 (0.135)		-0.314 (0.215)	-0.122 (0.296)		-0.0130 (0.196)	0.265 (0.173)		-0.449*** (0.141)	-0.377** (0.179)
Average per cent white		-0.00668 (0.00951)	-0.00130 (0.00904)		-0.00293 (0.00704)	0.000352 (0.00862)		-0.00319 (0.0137)	-0.000250 (0.0131)		-0.0139 (0.0120)	-0.00404 (0.0116)
Average population density		-0.000607 (0.000525)	-0.000430 (0.000648)		-0.000911 (0.000769)	-0.000691 (0.000868)		-0.000186 (0.000739)	-0.000162 (0.000852)		-0.000700** (0.000326)	-0.000414 (0.000417)
Northeast			-0.605 (0.455)			-0.590 (0.539)			-0.451 (0.564)			-0.772* (0.405)
Midwest			-0.547** (0.239)			-0.349 (0.300)			-0.577** (0.272)			-0.715** (0.304)
West			-0.782*** (0.255)			-0.799** (0.358)			-1.082*** (0.271)			-0.474 (0.392)
Constant	6.554*** (0.145)	23.75*** (6.690)	14.43* (7.599)	6.971*** (0.175)	25.43** (10.75)	15.74 (13.95)	6.267*** (0.160)	12.27 (10.12)	-0.983 (8.935)	6.427*** (0.168)	33.65*** (8.350)	28.50*** (10.50)
Observations	50	50	50	50	50	50	50	50	50	50	50	50
R-squared	0.083	0.236	0.378	0.083	0.181	0.278	0.058	0.175	0.329	0.035	0.297	0.410

Notes: Robust SEs in parentheses.
 *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

impact that JJ has on economic freedom and the extent to which an independent judiciary may help or hinder economic growth and prosperity, which should open up new avenues for future researchers to pursue.

Disclosure statement

No potential conflict of interest was reported by the authors.

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