Intergovernmental Cooperation in Planning and Financing Programs; An Outsider's Views*

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Mr. Chairman and friends: It is indeed a great pleasure for me to participate as the only foreign speaker in this conference which deals with one of the most pressing administrative problems of the United States. I deem it a distinct privilege to come into contacts with most able leaders and administrators as well as creative thinkers of Hawaii and the "Mainland." It is hardly necessary for me to add what a great delight it is for me to come back to your city, Mr. Mayor, and particularly on the campus of the East-West Center where I spent a most pleasant and fruitful time as a senior specialist a couple of years ago.

Mr. Chairman, my assignment is to add an international perspective to the intergovernmental cooperation in planning and financing programs which, according to the prospectus of the conference, include "the use of planning for coordinated use of funds made available through great-in aid programs between different levels of government and international assistance." You would readily agree with me that financial problems between the federal government and various states cannot be talked about in the same breath with these between different countries. Your conference moderator, Professor Fred Riggs whose imaginative capacity is known in many lands suggested when we met in Korea earlier this year that I might draw on my personal experience of some years ago as the budget director of a large aid-receiving country. I was aware that I would have to do this because I have no other background to fall

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back on that this, yet I was not sure how I could relate insights on **international** relations to the problem on **intergovernmental** cooperation.

So I turned to some current writings on the intergovernmental relations in your country. I do not have to tell you that I have been abundantly rewarded in this search: I have found that the grass is very green in this field and that many exciting new ideas come out with promise of good fruits in this field.

Now, with your permission, I would like to draw on some of these materials. I venture to do this with the hope that sometimes an outsider's view, however cursory it may be, may help crystallize the major issues under debates and dissect some of the solutions that are proposed by the proponents and contenders. At this session, we are to deal mainly with planning for financial cooperation between different levels of government.

Planning implies above all **priorities. Priorities** require clear identification of the main **problems.**

Further, financial planning involves not only finding **adequate ways and means** to finance programs but also **tayloring the right kind of financing for the right kind of problem.** Thus, our first task is to get at the right kind of problems.

As I read through the literature on the financial problems of intergovernmental relations, two major problems strike out: one is the plight of the central cities in the metropolitan areas, the other is the fiscal imbalance among the states. I find that these two problems are often mixed is discussion. Although the two problems are interrelated, a distinction between them could be useful in my view. While the problem of interstate imbalance touches only the poorer states, the metropolitan problem hits both the richer and poorer states because the plight of the central cities exist even within relatively rich states. Thus, among the two, the metropolitan problem seems, to an outsider, to be more prevalent and pressing.

The metropolitan problem in the United States seems to be at once natural and man-made. That is to say it is not only the result of urban growth but also the consequence of metropolitan fragmentation. This fragmentation of the metropolitan area into many jurisdictions gives rise to unequal distribution of fiscal ability among different municipalities. The consequence is the overburden of the central city, with an inevitable trend of exodus of richer citizens into the suburb, leaving costly citizens in the central cities. Any areawide solution is easily resisted by the higher-income municipalities in the area. Thus, a vicious circle develops. A study of the 29 municipalities in the Milwaukee metropolitan area done by John Shannon appearing

in a recent issue of National Civic Review is a good example.[1] Speaking on the fiscal plight of the central city, Shannon writes:

> "The central city is not only relatively short on tax resources, it is also long on expenditure demands. Its tax rate of almost $ 1.40 for strictly municipal type services——police and fire protection, health, sanitation and recreation ——is approximately five times greater than the average suburban municipal rate."[2]

The problem of fiscal imbalance among states is highlighted in a special lecture given by Professor Walter W. Heller of Minnesota at the Harvard Graduate School of Public Administration.[3] The findings on the interstate imbalance of this renowned economist, who was Chairman of the Council of Economic Advisors throughout President Kennedy's Administration and during the first year of President Johnson's show these three striking facts.[4]

First, on the revenue side the richest states raise twice as much revenue per capita from their own sources as the poorest states. In 1964, the five top states in terms of per capita revenue collections collected $ 396 per capita against $ 197 per capita in the five bottom states.

Second, in spite of this, the poor states make greater tax effort than the rich: while the ten richest states realized their revenue with only a 12-percent tax burden as a percentage of personal income, the ten poorest states drew their meager ration from a 13-percent tax burden.

Third, on the service and expenditure side, the wealthy states enjoy higher levels even with less tax effort: taking the average of the highest five and the lowest five states, the per capita expenditure level in 1964 showed a ratio of more than 2 to 1 in general expenditures and education respectively, approximately 3 to 1 in health and hospital and nearly 4 to 1 in public welfare.

What are than some of the major proposals for solution to these problem? Interestingly enough two Minnesota professors are the principal debaters in the field. They are Professor

1. John Shannon, "Striking a Balance: States Must Assist Metropolitan Area in Reducing Fiscal Disparities between Rich and Poor Jurisdictions," *National Civic Review*, Vol. LVII, No. 5(May 1968), pp. 238-242.
2. *Ibid*, p. 241.
3. Walter W. Heller, *New Dimensions of Political Economy: The Godkin Lectures At Harvard University*, Harvard University Press, 1966, Chapter Ⅲ."Strengthening the Fiscal Base of Our Federalism,"
4. *Ibid.*, p. 137.

Walter Heller whom I have already mentioned and Professor William Anderson, a very eminent scholar on local government. In brief, Heller proposes a revenue sharing plan; and Anderson calls it a myth and advocates an expansion of the grants-in-aid scheme. Let us examine this great Minnesotan and American detate in some detail below.

Professor Heller argues that the existing grants-in-aid scheme is not adequate to deal with the problem of interstate fiscal disparity. He shows that the average per capita receipt of grant-in-aid in a 10 poorest states in 1964 was $ 58 as against $ 85 per capita to the 10 richest states.

Beyond such grant-in-aid system geared to specified functions Mr. Heller proposes a revenue sharing plan to obtain greater equalizing effect among different states. Specifically, he proposes to take 2 percentage points of the federal individual income tax base and redistribute the money to all the states on a straight population basis. This would, on the basis of 1967 data, return $ 30 per capita to all of the states, yet the 2 percent would draw $ 24 per capita from the ten richest states and only about $ 18 from the ten poorest. In effect, this is an interstate income redistribution plan. Obviously, this is a policy proposal with a high degree of fiscal policy orientation.

Professor Anderson counters Dr. Heller's proposal in an article in the recent *PAR* Symposium on Intergovernmental Relations.[5] Among the myths which Anderson ascribes to a federal tax sharing schemes such as Heller's are: (1) the myth of the national treasury's rolling needed revenue surplus; (2) the myth that all the states have reached the absolute limit of their ability to find and raise additional revenues for the support of their own public services. As you can see, Professor Anderson is a great champion of fiscal integrity at the state as well as at the federal level. One important caveat Anderson raises about Heller's argument is on the unrestricted nature of the revenue to be shared by the states. Anderson fears that the unconditional fund such as this would be pumped to the states under a tax sharing plan might not guarantee the proper pass-through to the local communities which are in greatest need of money particularly the overburdened central cities in metropolitan areas.

To such a proposal, Anderson's alternative is increasing the grants-in-aid by the same amount of new revenue accruing to the states, while allowing the recipient states to reduce their matching contributions by similar amounts in order to enable the states to have more unrest-

5. William Anderson, "The Myths of Tax Sharing," *Public Administration Review*, Vol. XXIII, No. 1, (January/February 1968), pp. 10-14.

ricted funds of their own to spend on non-aided functions.

Anderson's caveat is echoed by some others who have done empirical researches on the fiscal behaviors of states and municipalities. Two recent studies on state and local fiscal system done by Korean scholars teaching in the United States, Drs. Yong-Hyo Cho and Woo-Sik Kee, were reported in a recent *PAR* issue and shed some light on the question as to what determines the relative fiscal assignment—revenue and expenditure—between a state and the localities.

The first of these by Dr. Cho bears out that "inter-state or inter-local variation in policy outcomes, i.e., expenditures for various services and revenues from various sources" are not merely a "function of some socio-economic factors reflecting 'ability to pay' and the 'degree of demand' for public services," but depends also on "the nature of governmental or political systems."[6] In our present context, this means that funds made available to a state may not always get allocated on the basis of the degree of demand of the municipalities but may also be subject to the political scramble between various localities within the jurisdiction.

The second researcher, Dr. Kee, similarly observes on the basis of his findings that deviant cities are likely "the results of differences in state politics, ethnic and cultural background of the States," and concludes:

> "simplifying the complex world of State and local finance requires the State to relegate specific responsibilities to its local units of government."[7]

These serve a clear warning to unrestricted allocation of new funds to states without clear channels of pass-through to the local communities.

It appears that there has been considerable expectation that the new reapportionment system largely help achieve equity in the allocation of funds with the state. This hope was, for instance, explicitly expressed by Professor Heller.[8] But such as expectations is not sustained by actual results. A study by Prof. Alvin Sokolow, on the impact of reapportionment on California Senate, particularly its behavior on allocation of state fund, is a case in point.[9] According to Sokolow, a very interesting thing happened in the first session of the state senate

6. Yong Hyo Cho, "The Effect of Local Governmental Systems on Local Policy Outcomes in the United States," *Public Administration Review*, Vol. XXVII, No. 1 (March 1967), pp. 31-38.
7. Woo-Sik Kee, "State and Local Fiscal Systems and Municipal Expenditures," *Public Administration Review*, Vol. XXVII, No. 1(March 1967), pp. 39-41.
8. Heller, *op. cit.*, p. 160.
9. Alvin D. Sokolow, "The First Session: California Senate Holds Key to Long-range Impact of Redistricting on Legislative Policy and Personnel," *National Civic Review*, Vol. LVII, No. 5 (May 1968), pp. 243-48.

after the reapportionment. He reports that senators from the northern part of the state, who were in the minority for the first time because of reapportionment, still controlled the five top committees, plus the transportations Committee which controls the allocation of state highway construction funds and that these committee assignments determined many important policy outcomes. He cites an example in which one proposal which would have revised the formula for allocating state highway construction funds from a 55-45 to 60-40 split favoring the southern part of the state and which had been passed overwhelmingly by the Assembly, was killed in the senate transportation committee, controlled by senators from northern and rural areas. This researcher whose base is at the University of California at Davis concludes:

> "State legislatures have **internal cultures** and **persistent of behaving** that can frustrate intended changes introduced from the outside."[10]

Your moderator, **Dr. Riggs,** would call such a phenomenon and to a student of development administration it is interesting to note that this situation which is so prevalent in many developing countries also obtains in such a highly developed place as the State of California.

Mr. Chairman, I am not in a position to become a refree between two prominent Minnesotans, indeed two of the most eminent American thinkers on government policy and administration, rather I would like to go back to the point where I started and put major problems of intergovernmental financing in perspective. Let me state them again in simple terms.

Money is needed for the metropolitan problem, especially to alleviate the overburden of the central cities in metropolitan areas. Money is also needed to redress the fiscal imbalance among the states. The existing grant-in-aid system has been inadequate to redress the serious imbalance among the states. So a revenue sharing plan which would provide new funds to the states with slight income redistribution effect is proposed. But even with this bold approach, there is no guarantee that the general grants thus provided would pass-through the states to the most needed municipalities for the most needed purposes.

Part of the uncertainty stems from mixing of the issues, i.e., the metropolitan issue and the interstate inequality. People who look into the interstate imbalance are apt to rely too much on the aggregates and averages. Averages and intermediate future is the burning problem of the metropolitan center that cuts across all the states, poor or rich.

My humble suggestion is: divide the issue and apply different financial prescriptions to

10. *Ibid.*, p. 43.

different problems. To the metropolitan problem which requires recognition of the special needs of the central cities, more grants-in-aid may be the right kind of solution because this scheme is specially designed to deal with special problems of particular localities. To the interstate fiscal imbalance which is essentially a problem of general income disparity, a general-type grant with income transfer effect may be the right solution.

In the latter case, instead of involving all the states in a scheme as in a tax sharing plan, only a limited number of poorest states should be covered under a plan of selective general grants. Perhaps this is the area in which the United States experience in foreign aid could be of some help. "No string" should be attached to such aid. In view of the fact that the disparity between richest and pooest states are marked across all the service categories as we have observed earlier, such new funds should be entrusted with the recipient states without any conditions. Some poorer states could even use such money for part of the matching contributions to go with other federal grants-in-aid. This should be permitted.

Segregation of the issues and tayloring of the right kind of design to the right kind of problem is more easily said than done. Yet even in the realm of financing of creative federalism truth may lie in simplicity. Thank you.