

Federal grants-in-aid—solvency for state and local governments

Morton B. Millenson

Grants-in-aid from the federal government to state and local governments date from the nation's earliest days. Being sporadic, however, grants did not amount to much in budgets at any level of government until the Great Depression.

Until the 1930s most grants were for highways and schools. And although large sums went to the states for relief during the Depression, with the coming of the Second World War and the enormous increase in defense spending, the importance of the grants again faded.

Since the war, however, grants-in-aid have become so important that they are now a major factor in the financing of government

at all levels. In fiscal 1950 grants-in-aid made up just 5 percent of federal outlays and about 10 percent of state and local government expenditures. In 1977 they accounted for 17 percent of the federal budget and over 26 percent of state and local government budgets. And this growth is expected to continue.

General revenue sharing

Almost all grants-in-aid until 1972 were categorical grants that earmarked funds for very specific uses, leaving receiving jurisdictions little or no discretion in how the money could be spent. But with the introduction of general revenue sharing, states and

Distribution of federal grants-in-aid by function

Function	1962	Fiscal year					
		1967	1972	1976 (percent)	1977	1978e	1979e
Natural resources and environment	2	2	2	5	6	6	7
Agriculture	6	3	1	1	1	—	—
Transportation	36	27	15	14	12	12	12
Community and regional development	3	6	10	6	7	8	7
Education, training, employment, and social services	8	25	26	24	23	26	26
Health	5	10	17	18	18	16	17
Income security	38	25	26	18	18	17	17
General purpose fiscal assistance	2	2	1	12	14	12	11
All other	—	—	—	—	—	—	—
Total	100	100	100	100	100	100	100

e estimate.

— less than 0.5 percent.

SOURCE: Office of Management and Budget.

municipalities began receiving fairly large sums that could be used for almost any purpose, even to cut taxes.

In its original form, the revenue sharing program had more restrictions than when it was renewed in 1976. The biggest change has been that funds can now be used to cover a local government's share for other grants available only on a matching-fund basis. This means grant programs can now be financed entirely with federal funds.

As a result, general revenue sharing has become synonymous in the minds of many people with federal funding of state and local governments. Actually, it accounted for less than a tenth of the federal aid to state and local governments last year. And it is due to be

even a little less this year and next. It does seem, however, to have amounted to a permanent increase in federal payments to local governments, rather than a replacement for other types of grants.

It seems significant that the introduction of general revenue sharing in 1972 coincided with the end of an uninterrupted string of deficits in the operating accounts of state and local governments that (measured on the National Income Accounts basis) went back to 1948. There were deficits again during the 1974-75 recession, but substantial surpluses were recorded in 1976 and 1977, and surpluses seem likely in 1978. A few states with particularly large surpluses have cut taxes. And other states are considering reductions. Easing the tax burden in these states suggests a belief that responsibility for raising revenue has permanently shifted from state and local governments to the federal government.

State and local leaders seek more federal funding in the form of general revenue sharing. It gives them flexibility in fitting spending to their own views of local needs. While they have not gotten the increases they asked for, they have gotten more flexibility in some other programs. Most funds are still available only for narrowly defined uses, but there has been some loosening up. Funds that could be used, for example, only for streets and highways can now be used for mass transit.

How the grants are used

Every year for the past ten years, about a third of all grants-in-aid have been

Grants-in-aid programs exceeding \$2 billion during fiscal 1977

<u>Function and program</u>	<u>Department</u>	<u>Outlay</u> (billion dollars)
Natural resources and environment Sewage treatment plant construction	Environmental Protection	3.53
Transportation Federal aid highways (Trust fund)	Transportation	5.80
Community and regional development Community development block grants	Housing and Urban Development	2.09
Education, training, employment, and social service Elementary and secondary education	Health, Education and Welfare	2.34
Social services	Health, Education and Welfare	2.53
Employment and training assistance Temporary employment assistance	Labor	2.94
Health Medicare	Health, Education and Welfare	9.88
Income security Child nutrition and milk programs Public assistance-maintenance	Agriculture Health, Education and Welfare	2.78 6.35
General purpose fiscal assistance General revenue sharing	Treasury	6.76

SOURCE: Office of Management and Budget.

under programs for payments to be made to individuals through state and local agencies. Most have been programs calling for state or local governments to match federal funds with money of their own. But some call for local governments to furnish only administrative services.

These payments to individuals fall under a number of the functional areas into which federal expenditures were divided by the Congressional Budget Act of 1974. And as a result, the magnitude of total spending is not apparent when the grants are broken out by function.

In the early 1960s, *transportation* and *income security* were by far the most important functions. Together, they accounted for almost three-fourths of the funds granted. They are still important, but the distribution of funds has changed drastically since then.

The biggest function today—*education, training, and social services*—is itself the aggregation of a large number of programs that together cost \$15.8 billion in fiscal 1977. Among these programs are four that cost the government over \$2 billion: *elementary and secondary education, social services, employment and training assistance, and temporary employment assistance*. None of these

programs or any of the others costing over \$2 billion in 1977 are budgeted at lower levels in 1978 or 1979.

How Seventh District states fare

Together the five states of the Seventh Federal Reserve District received \$9.42 billion in fiscal 1977. That was about 14 percent of the \$67 billion distributed to the 50 states and the District of Columbia. As these five states had a little over 15 percent of the population, their combined per capita allotment (\$283) was below the national average of \$314.

The national figure is somewhat distorted by the very high per capita payments to the District of Columbia (\$1,365) and Alaska (\$938). Vermont had the next highest payment relative to population (\$461). All other states received payments between the amounts for Vermont and Indiana (\$205).

Illinois received \$3.2 billion, the fourth largest payment to the 51 governments. Its per capita payment (\$284), however, was about average for the five states of the district.

Reasons for the spread in the per capita distribution of grants-in-aid between the five states are hard to pinpoint. It is particularly hard to see why Indiana received proportionately the least of any state.

The two areas where Indiana seems particularly low for its population are in grants for highways and urban mass transit. But these two areas do not in themselves account for the big difference between Indiana and the other four district states. Since many programs are voluntary and require matching funds, the difference could be that Indiana and its constituent local governments simply chose not to participate on the same scale as other states in the district.

Grants-in-aid to district states

<u>State</u>	<u>1977 population¹ (thousands)</u>	<u>Rank</u>	<u>1977 grants received (million dollars)</u>	<u>Rank</u>	<u>1977 grants received per capita (dollars)</u>
Illinois	11,245	5	3,202	4	285
Indiana	5,330	12	1,095	22	205
Iowa	2,879	25	714	31	248
Michigan	9,129	7	2,915	5	319
Wisconsin	4,651	16	1,493	12	321
Total five states	33,234	—	9,419	—	283
Total U.S.	216,332	—	67,083 ²	—	310

¹Provisional estimates, 50 states and District of Columbia, July 1, 1977.

²Excludes grants to Puerto Rico, Virgin Islands, American Samoa, Guam, and Trust Territory of the Pacific.

SOURCE: Bureau of the Census, U.S. Treasury.