July 31, 1992

HOW WASHINGTON BOOSTS STATE AND LOCAL BUDGET DEFICITS

INTRODUCTION

While Americans for many years have been accustomed to reading stories in the press about huge federal budget deficits, more recently they have seen news stories lamenting record state budget deficits as well. In 1991, the combined deficits of 31 states totaled over $30 billion.[1] New York and California alone accounted for $19 billion of that amount. Local governments are suffering similar budget problems. Nearly 40 percent of all counties with populations over 100,000 faced budget shortfalls in 1991.[2] Cities also were affected. Bridgeport, Connecticut, almost filed for bankruptcy, and Philadelphia, Pennsylvania, found its credit rating lowered to junk bond levels. While some state budgets show improvement this year, the underlying problems remain.

Some analysts claim that these record deficits occur because state taxes are too low. Yet three of the five states with monster deficits, New York, California, and Connecticut, are also among the top ten states in per capita taxes.[3] Other analysts point to a high rate of spending as the cause of deficits, and this indeed seems to be significant. Eight of the ten biggest spending states in the 1980s faced deficits in 1991.[4]

Harming States. This year, many states used accounting gimmicks, higher taxes, and some spending restraint to trim their deficits. But budget cut debates often have focussed on police, teachers, and essential services. And in the long run, higher taxes

1 "The Sad State of the States," *Business Week*, April 22, 1991, p. 24. Also see "State-Local Finance: Rethinking Service Delivery at Taxing Authority," *The Fiscal Newsletter*, March/April 1992, p. 1.

2 National Association of Counties, *County Government Budget Shortfall Report*, August 1991, p. 3.

3 Advisory Commission on Intergovernmental Relations, *Significant Features of Federalism, Vol. 2*, 1991, pp. 164-165; *Business Week, op. cit.*

4 Stephen Moore, "State Spending Splurge: The *Real* Story Behind the Fiscal Crisis in State Government," Cato Institute *Policy Report*, May 23, 1992, p. 9.

will reduce the productivity of businesses in these states, and the purchasing power of consumers, which will make local economies worse and reduce tax revenues.

States therefore must find ways to restrain or cut spending in non-essential areas. But one important obstacle to spending restraint largely has been overlooked: Federal government grants-in-aid and mandates essentially force state and local governments to spend much more than necessary on everything from medical care to welfare to road building. A complex web of federal programs binds together the treasuries of federal, state, and local governments. As much as 25 percent of state budgets now comes from the federal government, and up to 60 percent of some state budgets is spent on joint federal-state programs. Among the most important joint programs are Medicaid, which will cost the states $44 billion in 1992, and various federal welfare mandates, which will add $15 billion to state budgets.

Most state and local officials welcome this financial assistance from Washington—even though the money comes from the very same people who pay state and local taxes. But the problem is that the money comes with strings attached. To obtain it, the states and local governments must also spend funds, and abide by costly federal rules, that also push up spending.

Federal government assistance leads to higher budget costs on the states and local governments through two principal mechanisms: grants-in-aid and direct mandates.

Grants-in-aid provide funds to the states to achieve certain federal ends. The states themselves must contribute a certain amount of their own funds for the project in question and abide by federal guidelines and regulations. So-called block grants, which combine money for several specific programs within one large, more flexible grant, impose looser constraints on the states. For example, the Social Services Block Grant requires states to use funds to help prevent child abuse and to support emergency food and shelter programs, but does not prescribe exactly how the state must do this. Other grants, such as federal Medicaid funds or drug treatment grants, place very strict requirements on how the states must spend the funds.

There are currently over 500 grants-in-aid programs to states and localities. The total cost of these programs to the federal government has grown from $10.9 billion in 1965 to $171 billion this year. Estimates for total state costs run as high as $75 billion.[5] The cost to the state and federal governments combined of Medicaid mandates alone has grown from $5 billion in 1970 to a probable $104 billion this year, with spending for 1995 projected at $200 billion.

Grants-in-aid boost state spending in a number of ways:

✓ States accepting money for a construction project, for example, a subway, usually will be left to cover the project's huge operating costs;

5 This includes the states' contribution to Medicaid and Aid to Families with Dependent Children, as well as other health, income security, and other social services programs. It also includes transportation, agriculture, land management, conservation, environment, education, criminal justice, and occupational safety and health programs.

- ✓ States are induced to spend more money than they otherwise would, often driving up local as well as state taxes;
- ✓ When the federal government pays for a program administered by the states, the states have little incentive to run the program efficiently;
- ✓ States are induced to spend money on projects or programs that do not best serve the local interest.

Federal mandates simply require the states to provide certain services or programs. Unlike grants-in-aid, they do not help the states meet the expenses. These mandates include:

- ♦ "Crosscutting" requirements that are used to promote various federal policies through requirements on federal grants. For example, any construction project receiving federal funds must pay union-scale wages because the Davis-bacon Act requires "prevailing" wages to be paid, even if less expensive labor is available, thereby driving up the cost;
- ♦ "Crossover" requirements that force states to implement federal policy in one area or risk losing funds, usually in a related area. For example, states that fail to meet federal standards in licensing and testing school bus drivers could lose 5 percent to 10 percent of major federal highway grants;
- ♦ Direct orders that simply require states to conform with federal policy whether federal funds are involved or not. The Americans with Disabilities Act of 1990, for example, requires local governments to make all public transit accessible to the handicapped even when less costly alternatives are available that better serve the needs of the handicapped. In another example, the costs to the states and localities of complying with the federal Clean Water Act in the 1990s could reach $200 billion;
- ♦ Partial preemptions that allow the federal government to override existing state regulations. Some federal health and safety standards fall into this category.

The best way to cut the waste and the misallocation of resources caused by federal grants-in-aid and mandates is to return to the states the responsibilities that are best served by local governments. What is needed is a clear delineation of responsibilities, with the federal government handling national matters, such as defense and foreign relations, while state and local governments provide police protection, local infrastructure, and welfare. As important, state and local governments should not rely on the federal government for their funds for exclusively local functions. Rather, the federal government, in turning over responsibility for certain functions to the states, also must cut taxes by a corresponding amount. This will allow the states to raise taxes only enough to meet local needs, while cutting out the wasteful spending and inefficiency that come with federal government mandates.

To lift the current costly burden of federal mandates from the shoulders of the states, as well as to reduce federal spending and deficits:

1) **Congress** should limit itself to legislating on national issues. Programs aimed at state and local problems should be returned to those levels of government.

2) **Congress** should cut federal taxes by an amount equal to the cost of programs it returns to the state and local governments, thereby enlarging the tax base of those governments so they can pay for the programs.

3) **Federal mandates** should be fully funded and administered by the federal government.

4) **U.S. Senators** should be invited by their state's legislatures to explain the costs of newly proposed or enacted federal mandates to a special state joint legislative committee at the beginning and end of each session of the U.S. Congress.

The United States began as a federal system with state and federal governments sharing powers and responsibilities. The division of responsibilities was clear and rational. The shift in the past three decades toward federal involvement in nearly all areas of public policy has not been good federalism nor has it led in most instances to better results. Greater federal involvement has not raised education standards, held down health care costs, reduced traffic jams, or cut crime. States and cities are experimenting with new ways to provide education, welfare, infrastructure and other public services. Federal policy makers can help states and local governments to undertake innovative approaches by reducing federal red tape that raises their budget costs.

HOW GRANTS-IN-AID HAVE MUSHROOMED

The federal government's practice of giving money to the states to coax them into spending resources on federal policies began with the 1862 Morrill Act. This act authorized the transfer of federal land to the states which could then sell the tracts if they used the proceeds to fund colleges and universities.[6]

Federal grants grew significantly when Congress in 1916 authorized large-scale federal aid for state highway construction. This was followed by the Vocational Rehabilitation Act of 1920, designed to help disabled veterans, and the Sheppard-Towner (Maternity) Act of 1921, aimed at reducing maternal and infant mortality rates.

Franklin Roosevelt's administration greatly expanded the use of grants during the Great Depression. For example, the federal government spent billions of dollars on "emergency relief" programs, helping states to build highways, roads, and bridges. The Social Security Act of 1935 established numerous grant programs that continue today. These include old age assistance and aid to the blind and disabled, which are now completely funded by the federal Supplemental Security Income. In addition, the 1935 Act instituted aid to dependent children, as well as maternal health, child health, crippled children, and child welfare programs. These are now funded through the federal-state Aid to Families with Dependent Children partnership and related programs.[7]

6 Victor J. Miller, *A History of Federal Grants-In Aid to State and Local Governments* (Washington, D.C.: Federal Funds Information for States, June 24, 1988), p. 2.

After World War II, the primary focus of federal grants turned to urban issues. The federal government helped fund airport construction, urban renewal, urban planning, and the interstate highway system.[8] With the passage of the Great Society programs in the 1960s, the federal grant system exploded. The most important and far reaching of these programs was the 1965 addition of Medicaid to the Social Security Act. Medicaid is a program funded jointly by the states and the federal government. It provides medical aid to welfare families, the poor elderly, blind, and disabled. This one grant-in-aid program, which in 1970 cost a total of $5 billion, this year will cost the states $44 billion and the federal government $60 billion, for $104 billion in total spending.[9]

Reversing the Trend. From 1965 through 1980, the number of grant-in-aid programs quickly expanded to 538. During that period, the cost to the federal government grew from $10.9 billion to $91.5 billion. Hundreds of programs helped fund everything from nutrition for rural school children to housing for the urban elderly. Then, beginning in 1981, Ronald Reagan reversed this trend. As a start, under his Administration 57 individual grant programs were folded into seven block grants. The concept behind the block grant is to give more responsibility and flexibility to the states. Example: Instead of thirteen programs, each dealing with an aspect of education and each mandating precise uses for the money, under a block grant all of these programs would be rolled into one, and the states would be told, generally, to assess their local requirements and educate children in the way they thought best.

Block grants cut red tape and give states more flexibility. However, they also have a disadvantage. The most popular programs in Congress are those that allow a Congressman to take credit for solving a specific problem. With block grants, Congress raises taxes so that state and local officials can claim credit for programs.

How this undermines the block grant concept is illustrated by two sets of legislation which were meant to help the homeless. In 1981 the Community Services Block Grant provided money to assist low-income individuals with housing and emergency aid. Additionally, the Social Services Block Grant provided money for emergency food and shelter programs. When, in 1987, homelessness emerged as a significant issue, Congress could have increased the block grants and let states deal with homelessness in their own way. Instead, Congress passed the multi-billion dollar Stewart B. McKinney Homelessness Assistance Act and created redundant and more expensive programs.

Symbolic Programs. Today, there are some 500 grant-in-aid programs. Most cost less than $10 million per year. These smaller programs were created more to symbolize the desire of Washington lawmakers to "do something" about certain problems, than to have any significant impact. Example: In-home Services for Frail Older Individuals, created in 1988, is meant "To provide grants to States for in-home services for... victims of Alzheimer disease and related disorders...."[10] But the budget obligation for fiscal 1992 is only $6.8 million, or an average of $136,000 for each state—hardly enough to be of any real help.

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8 Miller, *op. cit.*, p. 3.

9 House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs, 1991 Green Book*, p. 1416.

10 CFDA 93.641, Special Programs for the Aging—Title III, Part D—In-home services for Frail Older Individuals.

HOW GRANTS-IN-AID WASTE MONEY

Grant-in-aid programs create incentives that lead to wasteful spending at all levels of government. The federal government wastes money because the states' contribution to each program reduces the explicit cost of a program to Congress. This is in spite of the fact that taxpayers must pay for the entire cost at one level of government or another. Because Congress does not pay the full cost of the program, a grant-in-aid program appears a better value for the money than if the program were paid for entirely out of federal funds. This in turn means that Congress creates many programs requiring a state contribution that federal lawmakers would consider uneconomic or wasteful if Washington were responsible for all of the funds.

The lure of federal funds also encourages states and localities to support and participate in capital projects they never would undertake if they had to rely on their own money.

This causes four problems:

1) **States or localities accept money** to build a project, such as a subway, but are left on their own to pay operating expenses after the project is completed.

2) **Federal matching formulae** give the impression of a "buy one, get one free" sale. States are encouraged to spend more money than they otherwise would, driving up the cost for their citizens and the federal taxpayer.

3) **States have little incentive** to administer effectively a program paid for by the federal government when little of its own money is at risk.

4) **The promise of federal dollars** induces states to spend money on projects that do not serve local needs as well as alternatives might.

Various grant-in-aid programs illustrate the perverse nature of these spending and management incentives.

Example: Mass Transit Systems. Consider the Miami light rail system, known as Metromover. It opened in 1984, and was funded mainly through a grant under the Urban Mass Transportation Act. Planners bragged that 100,000 people would ride Metromover each day; they claimed the daily ridership would top 200,000 by 1985. When ridership proved to be only around 10,000 people a day, President Reagan remarked that "it would have been a lot cheaper to buy everyone a limousine."[11] History is repeating itself today as Los Angeles builds a subway system, largely funded by the federal government. The estimated cost is $1 billion a mile. The system eventually will open in downtown Los Angeles, but does not extend to the suburbs, where the bulk of Los Angelinos live. Thus it will have a minimal effect on traffic problems.[12]

Cities like Miami and Los Angeles press for such systems in large part because they do not pay the full cost. Thus, from a narrow, local point of view, wasting billions of

11 Doug Bandow, "How Federal Aid Raises State and Local Spending," Cato Institute *Policy Report*, November/December 1989, p. 10.

12 *Ibid.*

dollars on a huge project can make good economic and political sense if someone else is picking up a large share of the bill. Writes George Peterson, Director of the Urban Institute's Public Finance Center, "...if forced to become reliant on their own resources, states would select very different budget priorities than those coaxed from them by federal aid."[13] In fact, one survey of municipal projects receiving partial federal and state assistance found that 51 percent of the projects would not have been undertaken without federal aid.[14]

Example: Welfare. Aid to Families with Dependent Children (AFDC) and Medicaid for the non-elderly poor are two of the most expensive components of America's welfare smorgasbord, costing about $130 billion in 1992. States share these costs with the federal government according to congressionally determined formulae. States pay as much as half of AFDC and almost 45 percent of Medicaid.

These programs suffer from the "buy one, get one free" temptation that induces some states to provide broader coverage than they would if they were spending only their own taxpayers' money. States are largely free to set different levels for AFDC payments. Example: In Mississippi the maximum annual grant for a family of three is $1,440 a year, while in California the maximum payment is almost $8,000.[15] The federal aid to Mississippi is much less than that given to California. Nevertheless, in their federal tax payments frugal Mississippians must help fund California's "generosity."

Similarly, with Medicaid states have the option of providing non-essential services and sharing the costs with the federal government. Forty-seven states pay for dental coverage, 28 for occupational therapy, and 29 for chiropractor's services. More services cost more money, which comes from both state and federal taxpayers. In addition, for a variety of reasons including efficiency, cost of living, and types of patients served, the average recipient cost varies widely. New York costs are $5,099 per recipient while the costs in West Virginia are only $1,443. If all states delivered Medicaid as cheaply as West Virginia, the nation's Medicaid bill would be cut by 53 percent or some $38 billion per year.[16]

Example: Job Training Partnership Act. When one level of government pays and the other spends, there is little incentive for the spending party to spend wisely. This is documented in a General Accounting Office report on the Job Training Partnership Act (JTPA). JTPA is a $4 billion a year block grant program where a "block" of money is sent to each state with general guidelines on how to spend it, rather than precise regulations.

The goal of JTPA is to train and find jobs for poor people and dislocated workers. Yet the GAO report found a number of problems with the program's effectiveness. Among them: contrary to law, too much money goes to retrain the most employable workers instead of those most in need; in some instances only 60 percent of the placed

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13 George Peterson, "Federalism and the States," in John Palmer and Isabel V. Sawhill, eds., *The Reagan Record* (Washington, D.C.: Urban Institute, 1984), p. 244.

14 Catherine H. Lovell, et al., *Federal and State Mandating on Local Governments: An Exploration of Issues and Impacts* (Riverside, California: University of California, Riverside, 1979).

15 House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs*, 1992, p. 636.

16 House of Representatives, Committee on Ways and Means, *Overview of Entitlement Programs*, 1990 p. 1302.

workers kept their jobs for more than four months; as much as 30 percent of the cost of the program goes to overhead; some of the money was used improperly to lure corporations into locating in particular states; and, some of the money was used to purchase expensive equipment rather than to train people for jobs.[17]

The Most Costly Example of Grants-In-Aid: Medicaid

Medicaid is by far the most expensive of the grant-in-aid programs. Created in 1965 to assure health care to the poor, Medicaid cost $5 billion in 1970. This year Medicaid will cost $104 billion, with $44 billion paid by the states and $60 billion by the federal government. It is estimated by the National Association of State Budget Officers (NASBO) that Medicaid will cost almost $200 billion by 1996.[18] Medicaid consumes 14 percent of state spending.[19]

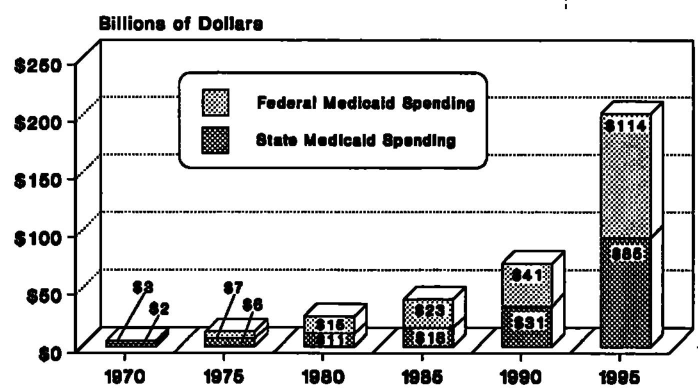
This huge and unanticipated rise in Medicaid's cost is due to the structure of the program itself, and particularly the feature that allows Congress to set many requirements that the states must fund.

When Lyndon Johnson signed Medicaid into law in 1965 as part of the Social Security Act, states received federal funds if they provided Medicaid services to poor children and their mothers, specifically, to recipients of federal Aid to Families with Dependent Children and to poor aged, blind, and disabled individuals, now generally recipients of Supplemental Security Income. States were allowed to expand the categories of eligibility beyond federal dictates, and they received matching funds for these additional recipients. Predictably, many states did so because they paid only part of the additional cost. This, of course, meant higher bills for federal taxpayers.

Outlays also went up because Congress could enact new mandates on states without the federal government being responsible for the full cost. In the 1980s, for example, Congress concluded that there were unacceptable disparities in eligibility criteria among the states, and decided to narrow them. Rather than side with the frugal states and restrict coverage, Congress repeatedly ordered broader coverage.

Chart 1

Total Medicaid Spending: An Increasing Burden on Both Federal and State Budgets



Source: National Association of State Budget Officers. Heritage DataChart

17 "Job Training and Partnership Act: Inadequate Oversight Leaves Program Vulnerable to Waste, Abuse and Mismanagement," General Accounting Office, July 1991.

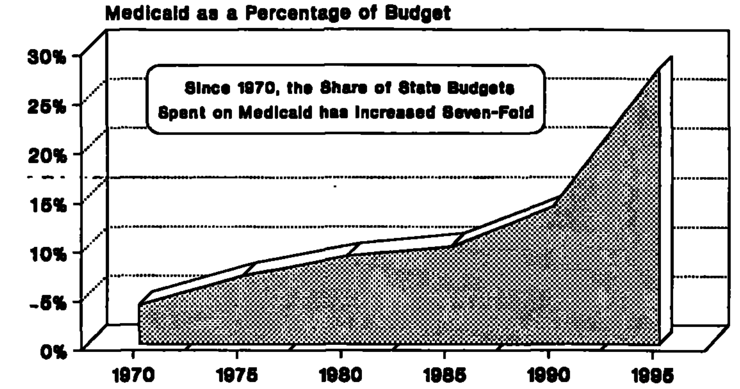
18 National Association of State Budget Officers, "Total Medicaid Spending," February 1992.

19 Statement by the National Governors Association, "Short Term Medicaid Policy," March 1991.

The most recent federally mandated expansion of Medicaid occurred in 1990. Among other things, Congress forced states to cover all children under the age of nineteen in families below the poverty level.[20] The previous year, Congress forced the states to provide Medicaid to pregnant women and children up to the age of six in all families below 133 percent of the official level of poverty.[21] These changes have proved very costly to the states.

Chart 2

By 1995, Medicaid Spending Will Consume Over a Quarter of State Budgets



Note: State spending base excludes local funds contributed to Medicaid programs.
Source: National Association of State Budget Officers. Heritage DataChart

Example: In Missouri, 80 cents of every new state dollar invested in the Missouri Department of Social Services over the last eight years has gone into Medicaid.[22] The latest federal mandates made the situation even worse, forcing Missouri to cut all state agencies 5 percent across the board, and put the savings into Medicaid.[23]

Example: California officials calculate that in order to comply with federal paperwork requirements mandated by the federal Nursing Home Reform Law of 1987, the state will have to increase Medicaid spending by between $400 million and $800 million.[24] John Rodriguez, deputy director of medical services at California's Department of Health Services, complains that "the new federal paperwork [will]... add nothing to the quality of patient care."[25] The state claims that its Medi-Cal payment system for nursing homes already substantially complies with the Nursing Home Reform Law. The major difference is that the federal paperwork is overwhelming. According to California health officials, one new federal form is 200 pages long compared to 40 pages for the equivalent state form.

HOW FEDERAL MANDATES INCREASE STATE SPENDING

In addition to the strings attached through grants-in-aid, the federal government uses regulation to exercise direct control over the states, usually by threatening to withhold money unless the states acquiesce to federal wishes. Often the money to be withheld

20 Omnibus Budget Reconciliation Act of 1990, P.L. 101-508.
21 Omnibus Budget Reconciliation Act of 1989, P.L. 101-239.
22 *State Health Notes*, February 1991.
23 *Ibid.*
24 Part of the Omnibus Budget Reconciliation Act of 1987.
25 "The Medicaid Budget Bust," *State Legislatures*, June 1991, p. 13.

has no direct connection with the federal mandate to be imposed. This type of coercion comes in four forms:

1) **Crosscutting Requirements** aim to achieve a social or economic goal and apply to all federally funded programs or projects. Example: The 1931 Davis-Bacon Act requires that locally "prevailing wages," in practice the union scale, be paid to construction workers on federally assisted construction projects—hospitals, highways, and housing. This increases the costs of federal projects by some $1.5 billion per year.

2) **Crossover Requirements** compel states to comply with requirements in one program or lose funding in a different program, but usually in a related area. Example: The Highway Beautification Act of 1965 required states to remove billboards from the nation's major highways or risk losing 10 percent of their highway funds.

   When states and localities complain about the costs of crosscutting and crossover regulations, some critics respond that they can avoid the costs by simply refusing the federal money. But this is does not tell the full story. If a state or locality were to reject federal regulation such as Davis-Bacon, and lose federal money for construction contracts, the loss to the state or locality would extend beyond the amount withheld by the government. The citizens would still have to pay their share of the federal taxes that fund Davis-Bacon projects in other jurisdictions. Federal spending and federal taxes have shrunk the tax base of states and localities to such an extent that they must go along with the federal regulation, because they lack the resources to raise enough funds on their own.

3) **Direct Orders** must be complied with under threat of criminal or civil penalties. Example: the Fair Labor and Standards Act that forces states to pay their workers the federally established minimum wage.

4) **Partial Preemptions** are where the federal government partially overrides a state's authority in the areas of health and safety. A program such as the Occupational Safety and Health Act is considered a "partial preemption" because the federal government sets minimum health and safety standards, but allows states or localities to administer and enforce the federal criteria.

The Most Costly Example of Regulation: Clean and Safe Water

The 1987 amendments to the Clean Water Act are among the most expensive examples of federal regulations. The Clean Water Act mandates that wastewater be cleaned at treatment plants before discharge into lakes and streams. The Environmental Protection Agency estimates it will cost $83.5 billion to bring all municipal wastewater treatment facilities into compliance with new national standards, and billions of dollars more to operate, manage, and maintain the plants. During the 1990s, state and local governments will spend over $200 billion to comply with current federal wastewater mandates.[26] The cost is so high that some cities, especially the poorer ones, may have to cut services like police, fire, and education to fund the federal mandates.

Local citizens and authorities might decide that their lakes and rivers, while not as clean as they would like, pose no serious health hazard. They might believe that the additional huge expense at a particular time is not worth the small improvement in water quality if this also means reduced police protection or lower teaching standards. Federal mandates, however, preclude local authorities from making those decisions.

Another expensive federal mandate emanates from the Safe Drinking Water Act Amendments of 1986, which promulgated new procedures and timetables for setting national drinking water standards. Standard & Poor's, the credit rating agency, predicts enormous costs stemming from the Clean and Safe Water Acts. It says the EPA has hinted that residential water bills could double to as much as two percent of median family income, that is, to $550 a year. History shows that Clean Water Act regulations, when added to Safe Drinking Water laws, are very expensive. Example: The federally mandated cleanup of Boston Harbor, largely to meet clean and safe water regulations, will result in an increase in the average Boston area residential water bill from the current $337 a year to $1,300 by the end of the 1990s.[26] Example: It might cost New York City between $4 billion and $5 billion to comply with only the Safe Drinking Water Act, over $500 per resident.[27]

Approaching $1 Billion. Few jurisdictions have thoroughly analyzed the potential costs of clean, safe water. One that has is Columbus, Ohio, a city of 633,000 with a metropolitan area population of over 1 million. That city found that the combined costs of complying with the Clean Water and Safe Drinking Water Acts will approach $1 billion—approximately $770 million for Clean Water and $105 million for Safe Drinking Water. The Columbus Health Commission estimates that compliance will cost each metropolitan area household an additional $685 per year throughout the 1990s.[28]

What impact will these costs have on cities? In its careful, almost diplomatic language, Standard & Poor's says, "...communities may have limited financial resources and many demands on these resources to provide services."[29] And, "The credit quality of [cities]... could be threatened, particularly where wealth indicators are weaker than average."[30] Should a city fail to meet Clean Water Act requirements, "regulators could ban additional sewer connections, stymieing a community's economic development, or impose stiff fines, potentially depleting cash reserves."[31] In other words, the poor will suffer because only the wealthy will be able to pay their water bills and also afford other services like garbage collection.

Although everyone favors clean and safe water, too few have asked whether the congressionally imposed standards are needlessly strict, driving up the cost on state and local taxpayers. Congress seems to care little about such an outcome because Congress does not have to raise the money to accomplish its goal. The question arises

26 "The Price of Clean, Safe Water," Standard & Poor's *Credit Comment,*, July 1990.

27 *Ibid.*

28 "Environmental Legislation: The Increasing Costs of Regulatory Compliance to the City of Columbus," Report of the Environmental Law Review Committee, City of Columbus (Ohio), May 13, 1991.

29 Standard & Poor's, *op. cit.*

30 "New Clean Water Costs Uncertain," Standard & Poor's *Credit Comment,* March 1991.

31 *Ibid.*

whether Congress would have found a cheaper or more efficient way to clean the nation's water if it had to spend federal tax dollars.

Another Expensive Regulation: Access to Public Transit for the Disabled

While Mayor of New York City, Ed Koch wrote a widely read article for *The Public Interest* magazine explaining the affect of federal regulation on state and local government. ~~Reacting to mandates from Washington,~~ Koch listed four maxims that appeared to guide the "mandate mandarins":

1) Mandates solve problems, particularly those in which you are not involved.

2) Mandates need not be tempered by the lessons of local experience.

3) Mandates will spontaneously generate the technology required to achieve them.

4) The price tag of the lofty aspiration to be served by a mandate should never deter its imposition on others.[32]

As an example of these maxims in practice, Koch discussed the crosscutting requirements of Section 504 of the Rehabilitation Act of 1973. He complained that the law mandates "total accessibility for the handicapped to transit *systems*, instead of dealing with the *function* of transportation: mobility."[33] That is, rather than work with New York to devise means for moving the handicapped around the city, federal regulations ordered the city to make public buses, subways, and subway stations accessible to the handicapped.

The regulations make little sense for two reasons: 1) they impose widely disparate burdens on different communities, and 2) handicapped people have different needs depending on their location and disability.

Enormous Transit System. New York City is unlike any other city in America. Its public transit system serves 5 million riders on a weekday. Most of them take the subway, which was designed and built around the turn of the century, but approximately 1.5 million people ride the buses. This is compared to a modern suburban jurisdiction with 100,000 public transit passengers a day served mainly by a small fleet of buses. The difference in size, age of the system, and type of system would argue for flexibility rather than the rigidity of Section 504.

The handicapped are not particularly well served either. Four million people work in the southern half of Manhattan, crowding the streets and making it difficult for wheelchairs to maneuver towards a bus or subway stop. In other parts of New York, long distances separate subway stops or bus stops, making them inconvenient for the handicapped, particularly in bad weather. The handicapped might have been better served if the city, rather than retrofitting the subways and buying new buses, instead used vans to provide door-to-door service.

32 Edward I. Koch, "The Mandate Millstone," *The Public Interest*, Fall 1980, p. 44.
33 *Ibid.*

Able-bodied commuters also suffer because of federal mandates meant to help the handicapped. If a handicapped person takes a bus, the driver has to get out to operate an expensive wheelchair lift in a process that takes about five minutes. If a handicapped person were waiting at each bus stop, this would turn a twenty minute ride into an hour-and-a-half ordeal for the other passengers.

Equally impractical rules apply to subway access. New York City's system was built in the early 1900s and riders enter almost exclusively by stairway. Federal mandates force costly retrofitting with elevators to accommodate the handicapped, forcing the city to spend money that could be better used elsewhere. In 1980, Koch estimated the cost of converting the system to conform to federal mandates at $1.3 billion over 30 years, plus at least $50 million in operating expenses.

Everyone Loses. To provide access for 22,800 people in wheelchairs and 110,000 semi-ambulatory people, Section 504 left New York City with the choice of either spending $1.3 billion to fix its transportation system, in a way unlikely to address the problem meant to be solved, or lose all its federal mass transit funding. In fact, everybody lost: The city unnecessarily will pay $1.3 billion. The handicapped will have access only to the regular mass transit system, which may not properly serve their needs. The people who commute by bus face long and unpredictable delays depending on the number of handicapped needing service. And, the federal mass transit funds buy less than they might have because they are paying for impractical transportation.

Mayor Koch estimated a cost of $38 per trip for each wheelchair user or severely handicapped person. Although it would have been cheaper to put them in taxicabs, the real point is that for substantially less money an alternative system, such as a van service, could have been instituted but for the mandates from Washington.

WHAT IS TO BE DONE?

Starting in earnest during the Great Depression, and continuing for about 35 years through the Great Society, Congress created a huge conglomeration of federal grant-in-aid programs administered by the states. In the last two decades, Congress increasingly has used its leverage to order states to fulfill national goals. Congress was helped in this effort by favorable Supreme Court decisions allowing Washington greater control over almost every aspect of state government. The result: The federal budget drives priorities and determines policies for all levels of government, while all levels of government face periodic budget crises.

The decline of federalism not only has been financially expensive, but also costly in ways difficult to measure. Government programs aimed at helping people too often have reflected a "one size fits all" mentality, ignoring both the differences among states and the benefits of experimentation.

To restore a balanced federal system, to preserve budgeting security, and to ensure that government programs are tailored to the needs of the people they serve, Congress must be removed from the state and local decision-making process. A number of steps would help achieve these goals.

1) **Congress should limit itself to legislating on national issues. Programs aimed at state and local problems should be returned to those levels of government.**

The federal government has taken over functions in recent years that the framers of the Constitution never would have considered "national" in scope. According to the Advisory Commission on Intergovernmental Relations, "by even the most lenient criteria of 'national purpose', it is impossible to justify many existing intergovernmental programs."[34] The report goes on to state that "The national government over time has acquired an array of functional and financial responsibilities that are more appropriately assumed by citizens at the state and local levels...."[35] Meanwhile, the report continues, "much of the present grant-in-aid money is in effect used by states and localities to shift their own financial burdens to a larger national tax base."[36]

Housing and medical care for the poor, and welfare, are problems that occur at the neighborhood level. They are the antithesis of national problems like national defense, international trade, interstate commerce, and polluted rivers and oceans.

2) **Congress should cut federal taxes by an amount equal to the cost of programs it returns to the state and local governments, thereby enlarging the tax base of those governments so they can pay for the programs.**

Gasoline, alcohol, tobacco, telephone, and other sales taxes provide $45 billion for the federal government. If the federal government divested itself of all sales taxes, that would allow the states to take in enough money to fund Medicaid without federal assistance, or more than enough money to fund Aid to Families with Dependent Children and federal housing programs.

The sales tax is traditionally a state and local levy and should remain so. It would make sense for the federal government simultaneously to divest itself of the taxes and the programs. In addition, Congress should cut the income tax to help states fund these programs.

By shedding as many inappropriate programs as possible, the federal government will save money. If states and localities want to maintain the federal programs, they can run them without interference from Washington at a substantial cost savings.

3) **Federal mandates should be fully funded and administered by the federal government.**

Any program that Congress believes is of national importance should be funded and administered through the national government. The experiment in administrative federalism, where Congress dictates and partially funds programs while the states administer them, has been a costly failure which has left voters confused about what level of government to hold responsible for the failure.

4) **U.S. Senators should be invited by their state's legislatures to explain the costs of newly proposed or enacted federal mandates to a special state joint legislative committee at the beginning and end of each session of the U.S. Congress.**

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34 *Devolving Federal Program Responsibilities and Revenue Sources to State and local Governments*, Advisory Commission on Intergovernmental Relations, 1986, p. 8.

35 *Ibid.*, p. 10.

36 *Ibid.*, p. 11.

Until the practice was changed by the 17th Amendment to the U.S. Constitution in 1913, U.S. Senators were elected by state legislatures and directly accountable to them. This arrangement helped the states fend off abuses of federal power. Today, U.S. senators still are the principal officials elected statewide and sent to Washington to represent the interests of their states. Given the huge burdens that federal mandates place on the states today, state legislatures would do well to demand formal and public reports from their two U.S. Senators on the effects of Washington policies on the states. State legislators would have the opportunity to question the Senators on what can be done to reduce the mandate burden and the public would be made better aware of why and how state funds are spent, often against their own wishes and priorities.

CONCLUSION

Progress often comes from recognizing mistakes and correcting them. The time has come to recognize that federalism, as it has evolved in the last seventy years, is badly off course. A correction must be made. Perhaps the most serious consequence of misguided federalism is the tremendous cost that federal mandates place on state and local budgets. Federal, state and local budgets face recurring crises unless Congress adjusts the relationship between Washington and the other levels of government.

The solution is to return to the states control of those policy areas that are best handled at a level of government closer to the people. This would include problems such as health, housing, and education. The federal government should handle truly national issues such as defense, trade, diplomacy, the environment, and immigration.

Time to Surrender. The current form of federalism is so cumbersome, wasteful, and expensive that the only practical solution requires the federal government to surrender to the states many of the programs under federal control, and provide the states the ability to pay for those programs by relinquishing federal control over the gasoline, alcohol, tobacco, telephone, and other excise taxes, and by reducing federal income tax rates so that states can tap that source if they desire.

At the end of his Presidency, Ronald Reagan declared that "while much of the 20th century saw the rise of the federal government, the 21st century will be the Century of the States."[37] The states today are the engine of domestic policy innovation. But unless Washington relieves them of onerous federal rules, their ability to solve America's domestic problems could be suffocated by red tape and mounting deficits.

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37 Ronald Reagan, "Flattening Hierarchies in the American Federal System," *Intergovernmental Perspective*, Fall 1988, p. 6.