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STATEMENT OF  
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BEFORE THE  
SUBCOMMITTEE ON INTERGOVERNMENTAL RELATIONS  
COMMITTEE ON GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
ON  
[ <sup>GAO</sup> GENERAL ACCOUNTING OFFICE VIEWS  
ON INTERGOVERNMENTAL ISSUES ]

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Mr. Chairman, we are pleased to be here this morning to share our views on the condition of our intergovernmental system. The past 20 years have seen an almost unbelievable growth in the scope and number of Federal assistance programs. This growth has defined federalism in a new context. Issues that were once considered the exclusive domain of State and local governments have, over the years, increasingly become national concerns.

As Federal assistance has grown to comprise 25 percent of State and local expenditures, the impact of Federal grant program constraints and conditions on State and local management and finances has become more pronounced. Collectively, the narrow boundaries of Federal categorical programs and the various mandates accompanying them have placed major strains on the accountability and administrative capacities of all three levels of government. The increasing interdependence of all three levels of government in the delivery of public services means that the Federal level cannot afford to ignore the impact of Federal policies on the ability of State and local governments to effectively manage Federal and non-Federal resources alike. While the period of growth in Federal assistance is probably over, the interaction among the levels of government will still be significant in determining public policy and designing public service delivery systems.

With fiscal constraints throughout the public sector as the likely scenario in the 1980's, the need for improved intergovernmental cooperation and coordination becomes critical and should serve as the impetus for the often called for, but seldom acted

on, improvements in the massive Federal aid system. Interest in reforming the way Federal assistance is allocated, regulated and administered is clearly increasing. The basic theme emerging is that every possible effort must be made to make better use of scarce public resources.

For the past several years, GAO has pursued an active inter-governmental work program, focusing on the impact of Federal grant policies and the need for grant reform. I should mention at this point that we have benefitted greatly from the very fine work of the Advisory Commission on Intergovernmental Relations. Our continuing dialogue with the Commission's highly expert staff has been invaluable to us in carrying out our work program.

One of our earliest reports in this area, "Fundamental Changes Are Needed In Federal Assistance To State And Local Governments," highlighted our long-standing position that the consolidation of fragmented and restrictive categorical grants into broader purpose programs is fundamental to improving the administration of Federal assistance programs at all levels of government. The categorical grant system has fostered an unwieldy and fragmented system for delivering public services. Further, categorical grants are often too restrictive to meet actual service needs at the State and local level and the burden of mounting a coordinated effort to deliver federally assisted services falls on the grantee. This causes management problems at the State and local level as grantees attempt to reconcile grant programs with separate and, at times, conflicting standards and requirements.

In addition to creating a variety of administrative problems, the proliferation of categorical programs has considerable impact on State and local priorities. By providing assistance in narrowly defined areas of national priorities, the Federal Government induces State and local involvement into programmatic ventures that they otherwise may not have funded from their own funds. Yet, because of matching and maintenance of effort requirements as well as the long-term costs which can be involved in operating federally assisted programs, State and local funds have also been enticed into these new areas. In this new era of State and local budgetary constraints, the dividend of fiscal growth is no longer available to cushion the cost impact of Federal grants. Localities in cut-back situations find that federally funded programs and basic services not eligible for Federal grants compete with each other for shrinking local dollars.

In a recent report, "Proposed Changes In Federal Matching And Maintenance Of Effort Requirements For State And Local Governments," we noted that localities facing budget reductions most often choose to continue their matching contributions to retain Federal grant funds while cutting, disproportionately, services funded solely from local revenues to maximize local budget savings while minimizing programmatic impact. As a result, a local priority shift towards federally funded programs occurs. We recommended that the Congress use matching requirements more sparingly and only where a specific Federal interest can be articulated. This would help restore State and local discretion in allocating their own funds.

Maintenance of effort requirements on the other hand, usually serve a clear Federal interest and need to be changed to more effectively prevent the substitution of Federal for State and local funds. However, we believe that maintenance of effort requirements need to be made more flexible to avoid penalizing or inhibiting bona fide State and local budget reductions.

Fiscal austerity has also provoked intensified concerns about the cost impact of Federal mandates on State and local governments. These mandates were imposed either by direct order or as conditions for receiving grants-in-aid. While State and local governments are technically free to reject grants with expensive mandates, it is highly unrealistic to expect them to do so.

To raise the funds needed for compliance, State and local governments can either raise taxes or distort their budgetary priorities by taking money away from State and local services not affected by Federal mandates. In either case, mandates can exert a profound influence on the ability of State and local governments to adjust taxes and spending in accord with State and local needs. This issue will likely become more serious as cuts in Federal aid are implemented. Very little is known about the prevalence of Federal mandating, the general magnitude of its impact, or the methods through which impact can even be estimated. We are beginning an effort to better define the problems and potential solutions.

Fiscal austerity also highlights the need to examine the ways in which scarce Federal dollars are allocated among States and localities. Despite the billions of dollars in Federal aid being

allocated by formula, no where in the Federal Government is there a coordinated, sophisticated, scientific approach to evaluate existing formulas. We are forming a small staff with the requisite technical skills in order to strengthen our ability to assist the Congress in assessing some of the complex issues associated with formula design.

We also see a need for increased attention to the issue of management control and accountability, as all levels of government must learn how to cope with reduced resources. As with most functions in our intergovernmental system, the task of achieving accountability for grant program management should be shared. There are strong and legitimate limits on the ability of the Federal Government alone to oversee and regulate grantee management of Federal funds.

In two recent reports, we advocated increased State and local oversight of Federal programs to better promote the accountability of these programs to the public and improve productivity. As a practical matter, however, State and local governments have little incentive to better manage and oversee Federal programs.

This is primarily a function of the inadequate rewards accruing to the State and local sector from effective management of Federal programs. We have identified two principal features of our system which contribute to this situation. First, the typical program is highly restricted in purpose and eligibility by federally developed standards and criteria. While the Federal level sees added control through such limitations, grantee oversight is discouraged when

they are given little discretion over program definition and scope. Secondly, most if not all dollar savings achieved through productivity improvements or reductions in program scope accrue to the Federal Government, not State and local governments. In fact, higher State spending is rewarded in over one-third of Federal formula grants.

Such features tend to exacerbate the inefficiency of federally assisted programs. The accountability of these programs to the needs and priorities of the State and local citizenry suffers as well. Insufficient oversight can also result in expensive duplication, conflict, and overlap between federally funded and State funded programs serving similar objectives.

In our report, "State And Local Government Productivity Improvement: What Is The Federal Role?," we recommended initiatives to remove barriers retarding State and local government productivity and an effort to incorporate positive incentives to reward effective management and improved productivity by State and local grantees. In our view, legislation such as the proposed Federal Assistance Reform Act and the recently enacted Paperwork Reduction Act are positive steps toward removing the barriers by streamlining, simplifying, and consolidating assistance programs. We also need to identify additional opportunities for incorporating positive incentives in assistance programs to recognize and reward improved productivity in grant program administration.

We have also urged that the Federal assistance system be changed to correct its tendency to discourage oversight by State

legislatures. While many legislatures have been increasing their oversight over Federal funds in recent years one of our recent studies showed that Federal assistance policies generally discourage legislative involvement by virtue of grant provisions delegating specific responsibilities for planning, program organization, and evaluation to State executive branches. We have recommended that the Intergovernmental Cooperation Act of 1968 be amended to ensure that these grant provisions not be construed as limiting or negating oversight by State legislatures. Not only would more active State legislative involvement increase accountability but the Federal Government would become more neutral with regard to internal separations of powers distinctions made by the States.

Prospects for improving the productivity of the intergovernmental grant system could also be enhanced if the costs and functions of administering Federal assistance programs were known and used to assess alternative approaches to delivering Federal assistance. In our report, "The Federal Government Should But Doesn't Know The Cost Of Administering Its Assistance Programs," we recommended that OMB take the lead to implement a Government-wide approach for accumulating, analyzing, and disseminating data on the financial and staff resources used in administering Federal assistance programs.

We have also encouraged and suggested initiatives to improve the audit of grant and assistance programs, including increased use of State, local, and private auditors to assist in the oversight

of Federal programs. We believe the single audit concept, advanced in our report, "Grant Auditing: A Maze Of Inconsistency, Gaps, And Duplication That Needs Overhauling," would go far in eliminating needless duplication of audits as well as gaps in audit coverage that arise through the uncoordinated audits carried out by each Federal agency. We feel that legislation is needed to give a statutory base to the important reforms initiated by OMB, with our cooperation, to administratively implement the single audit process.

In addition to the fiscal and accountability issues, sustained effort is needed in the area of standardization and simplification of program requirements. A number of important efforts have been undertaken in the past by both the Congress and the executive branch to promote standardization and central management guidance in the administration of Federal assistance, including passage of the Intergovernmental Cooperation Act of 1968 and development of several OMB management circulars defining standard administrative practices, cost principles, and audit procedures.

Passage of the Grant and Cooperative Agreement Act promoted a more recent wave of interest in simplifying guidance on the management of Federal programs. We are especially pleased that OMB has committed itself to a stronger, more active role in assistance policy management. We have continually supported a strong role for OMB as the primary agency for implementing reforms.

In summary, Mr. Chairman, we see grant consolidation, Federal mandates, better targeting of scarce Federal resources, and improved

oversight and accountability as the significant intergovernmental issues facing this Congress. We have strongly supported Congressional initiatives to reform the Federal grant process. In October 1979, the Comptroller General testified in favor of the Federal Assistance Reform Act of 1980 (S.878), which would, among other things, have established an expedited legislative process to consider grant consolidation proposals. We would hope that a similar measure will receive full Congressional approval this year.

While grant reform legislation is clearly necessary, we feel that Congress could also significantly improve Federal, State, and local relations by ensuring that intergovernmental implications are considered at the outset in the development of individual grant program legislation. Individual program requirements, which may appear to be justified separately on their own merits, may be viewed differently when their combined aggregate effects on the fiscal and administrative capacity of the intergovernmental system are assessed.

In a recent report, we suggested that the Congress establish a point of referral in each House to review and comment from an intergovernmental perspective on the matching and maintenance of effort requirements contemplated by proposed grant program legislation. Such a process could also be useful in the Congressional consideration of the full range of grant conditions and requirements, thus bringing about more consistency to our intergovernmental policies.

Mr. Chairman, that concludes my prepared statement. We would be pleased to respond to any questions.