# GAO

Testimony

For Release on
Delivery
Expected at
9:30 a.m. EDT
Wednesday
June 24, 1987

**Targeting Fiscal Assistance to
Reduce Fiscal Disparities**

Statement of
Charles A. Bowsher
Comptroller General
  of the United States

Before the
Subcommittee on Government Efficiency,
Federalism and the District of Columbia
Committee on Governmental Affairs
United States Senate
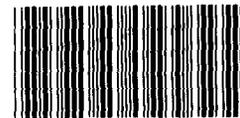
133287

039261 / 133287

Targeting Fiscal Assistance to
Reduce Fiscal Disparities

Summary of GAO Testimony

While general revenue sharing responded to the needs of the
1970's, today's fiscal environment has changed. Shrinking
federal aid to states and localities means that they are now
financing more of their public service needs from their own
resources. This has intensified the fiscal pressures faced by
local governments serving poorer communities whose taxable
resources make it difficult to adequately meet public service
needs. If the Congress decides that helping such governments
represents an appropriate use of federal funds, GAO believes that
targeting the assistance to communities that need it the most can
alleviate fiscal disparities at substantially less cost than
general revenue sharing.

The moderately targeted revenue sharing program reduced the
revenue gap between high and low income communities by
approximately 15 percent for $4.6 billion. A more targeted
formula could achieve the same 15 percent level of disparity
reduction for $2.4 billion. A highly targeted formula could
achieve a 25 percent disparity reduction for as little as $1
billion.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to talk about how the federal general revenue sharing program has helped fiscally distressed communities and why a more targeted approach to providing fiscal assistance would be better suited to today's fiscal conditions.

The general revenue sharing program was introduced during a period when the character of assistance to state and local governments was dramatically different than it is today. The early 1970's brought rapid increases in both the dollars and types of programs flowing from Washington to local communities. In this environment, revenue sharing not only helped communities with fiscal problems, but also gave them flexible monies that could be used to fill gaps in services not funded through other federal programs. In this context, general revenue sharing responded to the needs of the 1970's.

But today the environment has changed. General revenue sharing is gone, and federal aid to localities is shrinking not growing. Also, states have more flexibility to choose the mix of program services for their localities through various block grants. States and localities now have to finance more public services with their own funds. This, in turn, places a greater burden on governments serving poorer communities to maintain such services. In this new environment, two questions remain: What

is the magnitude of fiscal disparities? Can a program be developed that would alleviate fiscal disparities between high- and low-income communities at less cost than general revenue sharing. These are the topics I would like to cover today.

Let me begin by defining what we mean by fiscal disparities. Essentially, they are differences among communities in the taxable resources available and in public service needs. Given the same tax rate, a community with a lower economic resource base will derive fewer tax dollars per resident than a community with more taxable resources. Therefore, poorer communities must either accept lower levels of public services or tax themselves more heavily than their better-off neighbors in order to provide the same array and level of services.

Fiscal disparities among the nation's communities are substantial. As pointed out in our July 1986 report, we analyzed tax and income data for 38,880 units of local government in 3,134 counties across the United States. The data showed that, nationwide, cities, counties, and townships collected $264 per person in fiscal year 1983. However, local governments in the nation's wealthiest counties raised nearly $338 per person, whereas the poorest counties raised only $150 per person. These disparities are prevalent among governments serving both rural and urban areas. As shown in Chart 1, in the most rural counties, the lowest income communities required higher tax rates

to finance public services than did their higher income neighbors. However, this higher tax effort yielded 36 percent less revenue to meet public service needs.

For highly urbanized counties, we compared the revenue-raising capacity between central cities and their suburbs for the 20 largest metropolitan areas. Chart 2 shows a suburban revenue-raising advantage for 18 of the 20 largest metropolitan areas. For example, Cleveland's suburbs can raise $1.58 for each tax dollar collected by the central city. At the other end, the suburbs of San Diego can raise only 98 cents per tax dollar collected by the city. With this background, I would like to turn to how fiscal disparities can be reduced.

TARGETING FUNDS
REDUCES DISPARITIES

Targeting funds to lower income communities will reduce the disparities I have just described. Indeed, the more a given level of funding is targeted to low-income communities, the greater the reduction in disparities. In the same vein, greater targeting can achieve a given level of disparity reduction at lower cost.

Chart 3 shows the cost of disparity reduction based on three different targeting policies. Column 1 represents the most

3

targeted fiscal assistance formula. It limits eligibility to communities with incomes below the state's average which includes about half the U.S. population. Column 2 represents a formula that provides funding for communities with incomes up to 125 percent of the state's average. This would include about 90 percent of the U.S. population. Column 3 represents the least targeted formula; it provides funding for communities with incomes up to 150 percent of the state's average. This approach picks up about 99 percent of the U.S. population.

To provide a basis for comparison, I would like to first note that the general revenue sharing program provided about a 15-percent reduction in disparities at a $4.6 billion funding level, as shown in Column 3.

Column 2 shows that the same 15-percent disparity reduction can be achieved with $2.4 billion, almost half the revenue sharing funding level, using a more targeted formula. Column 2 also shows that $4.7 billion--about the same funding level as revenue sharing--could double the disparity reduction to 30 percent using this more targeted formula.

Finally, I would like to point out that even greater targeting can substantially reduce the cost of disparity reduction. Column 1 shows that a highly targeted formula providing funds only for communities with income below the state

4

average could reduce disparities by 25 percent with as little as
a $1 billion investment.

As you can see from chart 3, if funding is targeted only to
low-income communities, all of it contributes to reducing fiscal
disparities. On the other hand, if some funding is also provided
to high-income communities, funding for low-income areas must be
increased that much more to achieve a given disparity reduction.
This in turn raises the total cost of the program.

ADJUSTMENTS TO THE LOSS
OF FEDERAL REVENUE SHARING

Mr. Chairman, you asked us what impact the loss of revenue
sharing funds had on local governments. We have just started two
reviews to determine what kinds of service changes and fiscal
adjustments certain states and localities are making. A clear
picture of actual state and local impacts will have to await
completion of those efforts.

However, we do know that revenue sharing funds made up a
larger portion of local government budgets in poorer communities
than in wealthier jurisdictions. Therefore, poorer communities
clearly face a more difficult adjustment to the loss of those
funds.

Differences in the fiscal adjustments faced by county and
city governments are illustrated in chart 4. Column 1 shows that
counties whose average resident income is less than 75 percent of
the states' average income would have to raise local taxes by 16
percent to fully replace lost revenue sharing funds, almost twice
the national average of 8.3 percent. In contrast, the average
tax increase required in the highest income group would be 4
percent, or about half the national average. Column 2 shows that
the fiscal adjustment for cities would be somewhat less, but the
pattern is similar.

Finally, Mr. Chairman, you asked whether we believe there is
a need for a successor program to general revenue sharing for
fiscally distressed local governments. While local governments
serving low-income areas are at a marked fiscal disadvantage in
financing public services, the Congress must weigh the need for
such a program against other competing resource demands. If the
Congress decides that such an effort represents an appropriate
use of federal funds, we strongly believe that a program using a
highly targeted formula can alleviate fiscal disparities at
substantially lower cost than general revenue sharing.

Mr. Chairman, this concludes my statement. I would be
pleased to respond to questions.

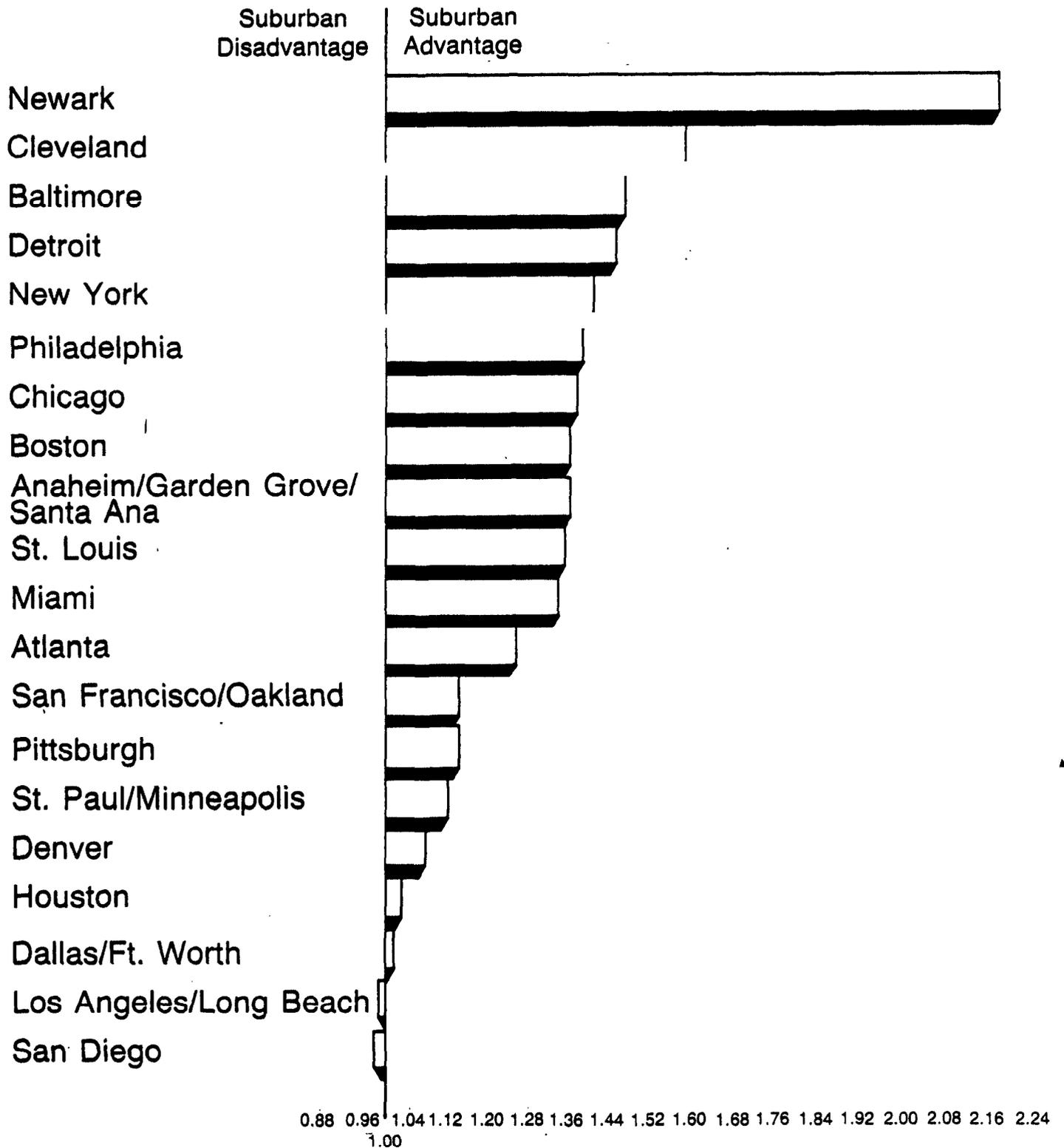# Chart 1: Fiscal Disparities Amor
Governments In Rural Counties

	Taxes as a Percent of Income	F Ta
Lowest Income Counties	2.33%	→
Highest Income Counties	2.14%	→
Ratio of Lowest to Highest	+9%	

Chart 2: Fiscal Disparities Between Central City and Suburban Governments

	Suburban Disadvantage	Suburban Advantage

Newark

Cleveland

Baltimore

Detroit

New York

Philadelphia

Chicago

Boston

Anaheim/Garden Grove/ Santa Ana

St. Louis

Miami

Atlanta

San Francisco/Oakland

Pittsburgh

St. Paul/Minneapolis

Denver

Houston

Dallas/Ft. Worth

Los Angeles/Long Beach

San Diego

0.88 0.96 1.04 1.12 1.20 1.28 1.36 1.44 1.52 1.60 1.68 1.76 1.84 1.92 2.00 2.08 2.16 2.24
1.00

GAO Chart 3: Cost of Reducing Fisc Disparities (Billions of Dollars)

DISPARITY REDUCTION %		INCOME ELIGIBILITY STANDARD (STATE AVERAGE = 100		
		100	125	1!
(1)	100	$3.9	$15.7	$3(
(2)	50	2.0	7.8	1!
(3)	30	1.2	4.7	(
(4)	25	1.0	3.9	:
(5)	20	0.8	3.1	(
(6)	15	0.6	2.4	⸢ ⸤
(7)	10	.0.4	1.6	:
		(1)	(2)	(

Chart 4: Increase in Taxes Nece
Offset the Loss of Revenue Sha

Percent of State Per Capita Income	Counties
75 or Less	16.2%
90 or Less	12.6
100 or Less	10.6
More Than 100	6.4
More Than 110	5.6
More Than 125	4.1
U.S. Average	8.3