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STATEMENT OF

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BEFORE THE

SUBCOMMITTEE ON INTERGOVERNMENTAL RELATIONS

SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS

ON

TARGETING FISCAL ASSISTANCE TO REDUCE FISCAL DISPARITIES

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here to discuss our report issued to you today on how targeting fiscal assistance could reduce fiscal disparities among local governments.

I would like to begin by defining what we mean by fiscal disparities. Essentially, we defined fiscal disparities as differences in the levels of taxable resources available to communities, and differences in public service needs among communities. Thus, 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 comunities must either accept lower levels of public services or tax themselves more heavily than their better-off neighbors to provide the same array and level of services. Similarly, communities requiring higher levels of services will have to tax themselves at higher rates than communities with lesser needs.

Fiscal disparities among the nation's communities are substantial. We analyzed tax and income data for 38,880 units of local government in 3,134 counties across the U.S. 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 compared to $150 per person in the poorest counties. Because rural areas tend to have lower income, some of this is due to urban-rural differences. However, disparities are prevalant within each group. For example, for the 40 percent of the U.S. population living in the most rural counties, those with the lowest income consistently devoted a greater percentage of their income to financing public services compared to their higher income neighbors. But, this higher

effort yielded nearly 40 percent less revenue to meet public service needs.

For highly urbanized counties, we compared the revenue-raising disparities between central cities and their suburbs for the 20 largest metropolitan areas. Chart 1 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've just described. The more a given level of funding is targeted to low-income communities the greater will be the reduction in disparities. Alternatively, more targeting can achieve a given level of disparity reduction at lower cost. For example, 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 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 disparity reduction.

Chart 2 shows the cost of disparity reduction based on three different targeting policies. Column 1 represents the most targeted fiscal assistance formula, limiting eligibility to communities with incomes below the state's average income--about half the U.S. population. Column 2 represents the formula used in your targeted fiscal assistance bill which provides funding for communities with incomes up to 125 percent of the state's

average--about 90 percent of the U.S. population. Finally, column 3 represents the least targeted formula, providing funding for communities with incomes up to 150 percent of the state's average--about 99 percent of the U.S. population.

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

Column 2, which reflects the formula used in your bill, shows that the same 15 percent disparity reduction can be achieved with $2.4 billion, almost half the revenue sharing funding level. Column 2 also shows that $4.7 billion--about the same funding level as revenue sharing--could double the disparity reduction to 30 percent.

Finally, I would like to point out that even greater targeting can substantially increase the amount of disparity reduction that could be realized. Column 1 shows that the cost of totally eliminating disparities just for communities with below average income could be achieved with $3.9 billion.

Increased Targeting Redistributes Funding Among Local Governments

Obviously, a key question will be how will greater targeting affect different communities? As I mentioned earlier, rural counties tend to have lower incomes compared to more urban counties. Consequently, increased targeting will allocate more funds to rural areas than the general revenue sharing program.

Indeed, the counties classified as 100 percent rural would receive almost 50 percent more funding under targeted fiscal

assistance than they would under the revenue sharing program with the same funding level. At the opposite end of the the urban/rural spectrum, targeted fiscal assistance payments to local govenments in those counties classified as 100 percent urban would be 94 percent of their revenue sharing payment. Chart 3 shows this trend for counties. The chart indicates that average payments to counties with 25 percent or more rural residents would be greater under the proposed targeted fiscal assistance formula in S. 2037. Conversely, counties with 75 percent or more urban residents would receive a lower payment.

While on the whole targeted fiscal assistance shifts funding to rural communities, it also targets more aid to low-income central cities in the largest metropolitan areas as opposed to those with relatively high incomes. Chart 4 ranks selected large cities according to their per capita incomes and compares payments they would receive under targeted fiscal assistance with what they would receive under the existing revenue sharing program. The lowest income cities would all receive increased funding while the highest income cities would get less.

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

CHART I
RATIO OF SUBURBAN TO CENTRAL CITY REVENUE RAISING CAPACITY FOR THE 20 LARGEST METROPOLITAN AREAS

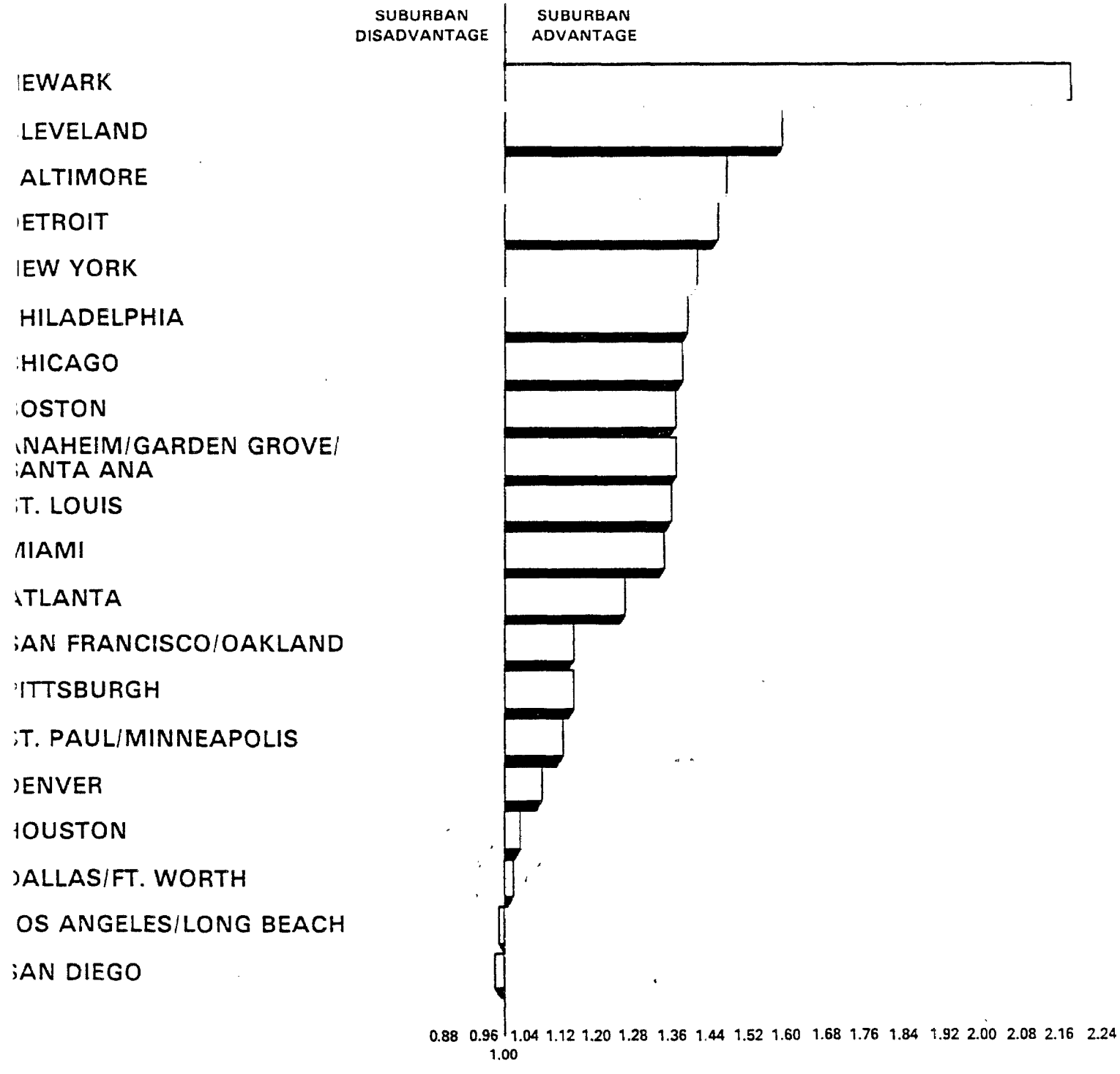

CHART II
ESTIMATED FUNDS REQUIRED TO ELIMINATE OR PARTIALLY REDUCE REVENUE DISPARITIES AMONG LOCAL GOVERNMENTS (BILLIONS OF DOLLARS)

	DISPARITY REDUCTION %	INCOME ELIGIBILITY STANDARD (STATE AVERAGE = 100)			
		100	125	150	
(1)	100	$3.9	$15.7	$30.6	
(2)	50	2.0	7.8	15.3	
(3)	30	1.2	4.7	9.2	
(4)	25	1.0	3.9	7.7	
(5)	20	0.8	3.1	6.1	
(6)	15	0.6	2.4	4.6	← GRS
(7)	10	0.4	1.6	3.1	
		(1)	(2)	(3)	

CHART III
RURAL AND URBAN AREAS: PERCENT CHANGE FROM GRS PAYMENT USING S2037 FORMULA

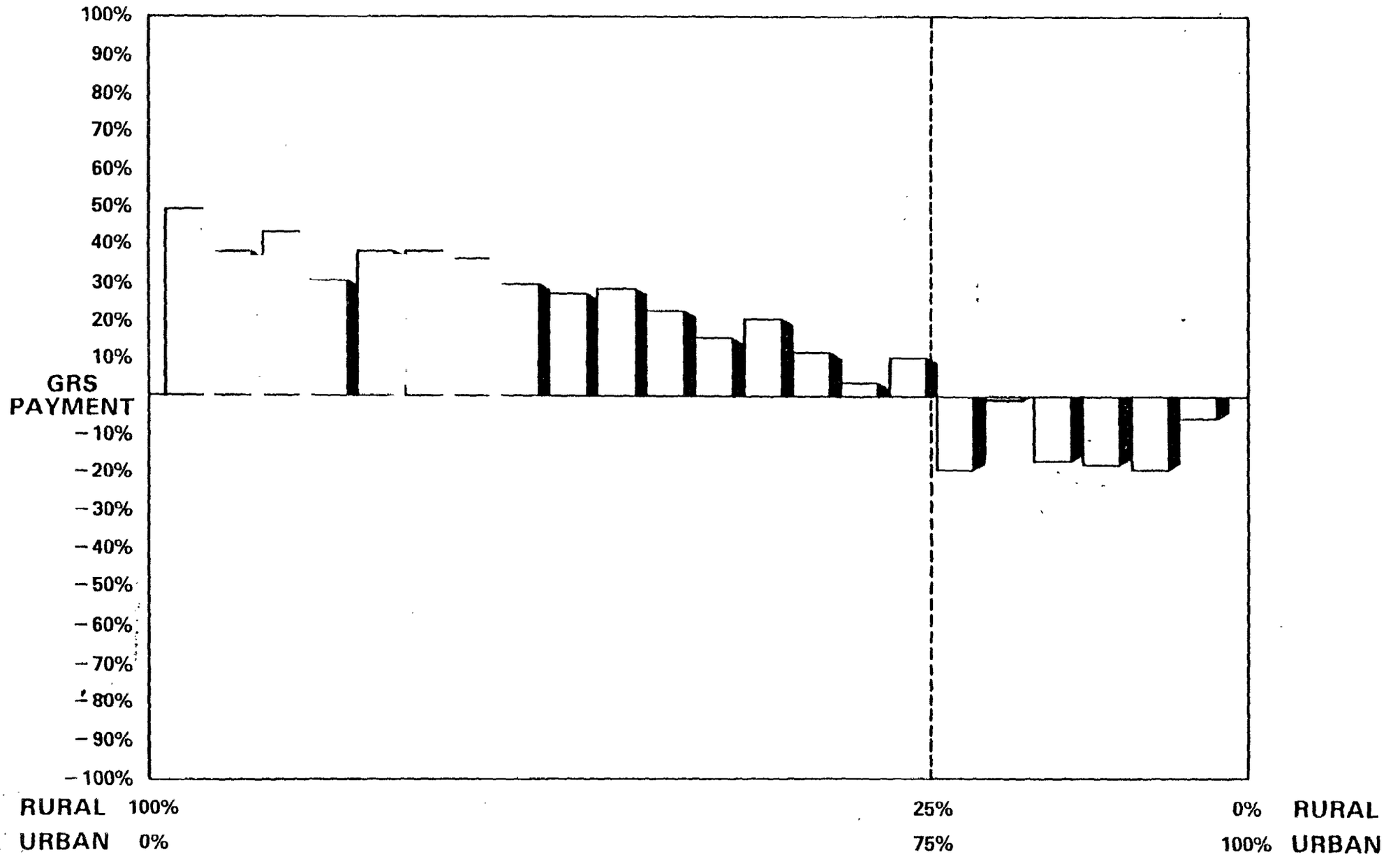

CHART IV
LARGE CITIES: PERCENT CHANGE FROM GRS PAYMENT USING S2037 FORMULA