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BLOCK GRANTS

Lessons Learned

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SUMMARY OF TESTIMONY BY LINDA G. MORRA
BLOCK GRANTS: LESSONS LEARNED

The Congress's interest in creating block grants from the fragmented multitude of federal categorical programs is not new. A 1949 commission report concluded, "A system of grants should be established based upon broad categories--such as highways, education, public assistance and public health--as contrasted with the present system of extensive fragmentation." In 1993, 578 federal categorical programs, with $182 billion in funding, provided assistance to states and localities.

FEW BLOCK GRANTS A total of 15 block grant programs, with funding of $32 billion, are in effect today, constituting 11 percent of the total federal aid to states. In 1981, the Omnibus Budget Reconciliation Act (OBRA) included the most substantial effort to consolidate federal programs by creating 9 block grants from about 50 of the 534 categorical programs in effect at that time. Funding for these programs was cut an average of 12 percent.

1981 BLOCK GRANT TRANSITION SMOOTH; SOME PROBLEMS AROSE
In general, the transition from categorical programs to block grants was smooth. In seven of the nine areas covered by the block grants, states had extensive experience from operating the categorical programs replaced by the block grants, which facilitated the transition. In these cases, states relied on existing management and service delivery systems. Our work showed that states used a variety of approaches, such as using carry-over funds from the categorical programs and adding state revenues, to help replace much of the funding reductions. Block grants also significantly reduced the number of federal reporting requirements, yet states reported that they maintained their prior level of data collection for their own management purposes. However, program data were often found to be unusable at the federal level because of the lack of comparability across states. Finally, even though block grants were intended to increase state flexibility, over time additional funding constraints were added, in part due to congressional concern that states were not adequately meeting national needs, in effect, recategorizing the programs.

LESSONS LEARNED Our research suggests that experience drawn from the experience with the 1981 block grants can teach us three lessons. First, there clearly is a need to focus on accountability for results, and the Government Performance and Results Act (GPRA) may provide the appropriate framework. Second, funding allocations based on distributions under prior categorical programs may be inequitable because they do not reflect need, ability to pay, and variations in the cost of providing services. Finally, states handled the transition to the 1981 block grants, but today's challenges are likely to be greater. The programs being considered for inclusion in block grants are not only much larger, but, in some cases, such as Aid to Families With Dependent Children, which provides cash assistance to the poor, they fundamentally differ from programs included in the 1981 block grants.

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the findings of our work related to consolidating categorical programs and turning them into block grants.

As you know, the Congress has become increasingly interested in proposals to reduce the potential fragmentation and duplication that the myriad categorical programs pose to states and localities. According to the Advisory Commission on Intergovernmental Relations, in fiscal year 1993, 578 federal categorical programs, with $182 billion in funding, provided assistance to states and localities. Creating block grants from federal categorical programs is not a new idea. In fact, a 1949 commission report concluded, "A system of grants should be established based upon broad categories--such as highways, education, public assistance and public health--as contrasted with the present system of extensive fragmentation."[1]

My testimony today will summarize the findings from a report we are issuing today prepared at the request of Congressman Goodling, Chairman of the House Economic and Educational Opportunities Committee, describing the 1981 block grants, assessing the experience of the states operating under these block grants, and presenting lessons learned that the Congress may find useful as it considers creating new block grants.[2] These findings are based on our earlier studies of the block grants created in 1981 and their implementation in 13 states and our more recent work on block grant programs in the health, education, and social services areas.[3]

In summary, we found that a total of 15 block grant programs, with funding of $32 billion, are in effect today, constituting a small portion of the total federal aid to states--$206 billion for 593 programs in fiscal year 1993. In 1981, as part of the Omnibus Budget Reconciliation Act (OBRA), 9 block grants were created from about 50 of the 534 categorical programs in effect at that time. In general, the transition from categorical programs to block grants was smooth.

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[1]Commission on the Organization of the Executive Branch, A Report to Congress on Federal-State Relations (Washington, D.C.: 1949)--from George E. Peterson, et al., The Reagan Block Grants: What Have We Learned? Washington, D.C.: The Urban Institute Press, 1986.

[2]Block Grants: Characteristics, Experience, and Lessons Learned (GAO/HEHS-95-74, Feb. 9, 1995).

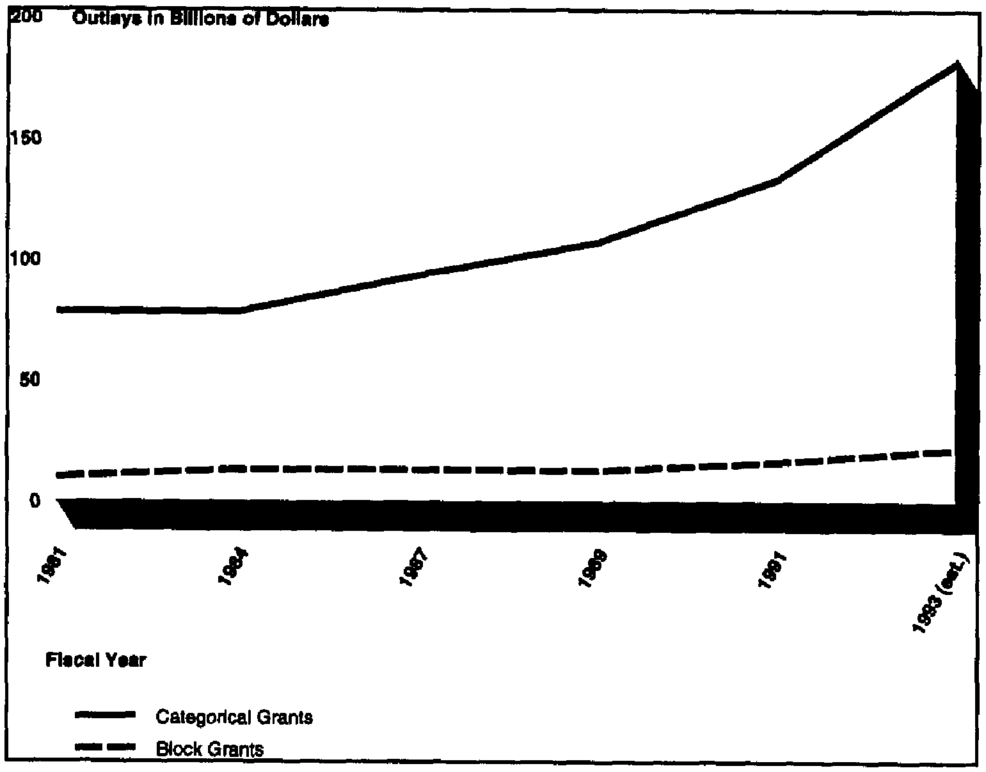
[3]Our look at the 1981 block grants, while extensive, covered 13 states that were varied but were not representative of the nation as a whole.

Our research suggests that experience with the 1981 block grants can teach us three lessons. First, there clearly is a need to focus on accountability for results, and the Government Performance and Results Act (GPRA) may provide the appropriate framework. Second, funding allocations based on distributions under prior categorical programs may be inequitable because they do not reflect need, ability to pay, and variations in the cost of providing services. Finally, the transition to block grants may be more challenging today than in 1981 because the programs being considered for inclusion in block grants are much larger, and, in some cases, fundamentally differ from programs included in the 1981 block grants.

CHARACTERISTICS OF THE 1981 BLOCK GRANTS

Block grants are broader in scope and offer greater state flexibility in the use of funds than categorical programs; in addition, block grants allocate funding on the basis of a statutory formula. Block grants have been associated with a variety of goals, including encouraging administrative cost savings, decentralizing decisionmaking, promoting coordination, spurring innovation, and providing opportunities to target funding. However, block grants have historically accounted for only a small portion (11 percent) of grants to states and localities, as figure 1 shows. Before OBRA created nine block grants in 1981, three block grants had been created under the Nixon administration for community development, social services, and employment and training. More recently, the largest block grant program in terms of funding was created in 1991, the Surface Transportation Program.

Figure 1: Block Grants Are Small Portion of All Grants



Source: U.S. Advisory Commission on Intergovernmental Relations.

OBRA Created Nine Block Grants

OBRA changed substantially the administration of many federal domestic assistance programs by consolidating more than 50 categorical grant programs into nine block grants and shifting primary administrative responsibility for these programs to the states. The OBRA block grants carried with them significantly reduced federal data collection and reporting requirements compared to the previous categorical programs, although some minimal requirements were maintained to protect federal interests.

Overall federal funding for the block grants in 1982 was about 12 percent below the 1981 level for the categorical programs. However, changes in federal funding levels for the block grants varied by block grant--ranging from a $177 million or 30-percent reduction in the Community Services Block Grant (CSBG), to a $94 million or 10-percent increase in the Community Development Block Grant (CDBG). The Social Services Block Grant was reduced by the largest amount--$591 million, representing a 20-percent reduction.

States received broad discretion under block grants to decide the specific services and programs to provide, as long as they were directly related to the goals of the grant program. Four of the block grants were for health, three for social services, and one each for education and community development.

The three existing block grants were (1) the Health Incentives Grant for Comprehensive Public Health, which was incorporated into the Preventive Health and Health Services Block Grant; (2) the Title XX Block Grant, which was expanded into the new Social Services Block Grant; and (3) the Community Development Block Grant (CDBG), which had been in existence since 1974. Under OBRA, states received CDBG funds to allocate to cities with a population under 50,000. In two cases (Primary Care and Low-Income Home Energy Assistance), a single categorical program became a block grant.

Funding and Other Requirements Viewed as Less Onerous

States generally viewed the funding and other federally imposed requirements for the 1981 block grants as less onerous than those for the categorical programs. Funding requirements were used to (1) advance national objectives (for example, to provide preventive health care or, more specifically, to treat hypertension); (2) protect local service providers who historically played a role in service delivery; and (3) maintain state contributions. Set-aside requirements and cost ceilings were used to ensure that certain services were provided. For example, the Preventive Health and Health Services block grant required that 75 percent of its funding be used for hypertension. A limitation in the Low-Income Home Energy Assistance Block Grant specified that no more than 15 percent of funds be used for residential weatherization. Pass-through requirements--notably the requirement that 90 percent of 1982 allocations under the Community Services Block Grant be awarded to community action agencies--are used to protect local service providers. The community action agencies were the primary service providers under the prior categorical program. Finally, provisions were included to maintain state involvement by preventing states from substituting federal for state funds.

Data Collection and Reporting Requirements Reduced

Block grants carried with them significantly reduced federal data collection and reporting requirements compared with categorical programs. Under the categorical programs, states had to comply with specific procedures for each program; block grants had only a single set of procedures. Federal agencies were prohibited from imposing burdensome reporting requirements and, for many of the block grants, states were allowed to establish their own program reporting formats. However, some data collection and reporting requirements were contained in each of the block grants to ensure some federal oversight of block grant administration.[4] Block grants generally require the administering federal agency to report to the Congress on program activities; provide program assessment data, such as the number of clients served; or conduct compliance reviews of state program operations. Basic reporting requirements were also required of state agencies.

EXPERIENCE OPERATING UNDER THE 1981 BLOCK GRANTS

In general, the transition from categorical programs to block grants following the passage of OBRA was smooth, and states put their own imprint on the programs. For the most part, states could rely on existing management and service delivery systems. States consolidated offices or integrated service delivery under related programs. State officials generally found federal requirements under the block grants created in 1981 less burdensome than those of the prior state-operated categorical programs. Moreover, states reported that reduced federal application and reporting requirements had a positive effect on their management of block grant programs. In addition, some state agencies were able to more productively use their staffs as personnel devoted less time to federal administrative requirements and more time to state-level program activities.

Although states realized considerable management efficiencies or improvements under the block grants, they also experienced increased grant management responsibilities because they had greater program flexibility and responsibility. Measuring the net effect of these changes in state responsibilities on the level of states' administrative costs is impossible. Such cost effects cannot be quantified because of the absence of uniform state administrative cost definitions and data as well as a lack of comprehensive baseline data on prior categorical programs.

States took a variety of approaches to help offset the 12-percent overall federal funding reduction experienced when the categorical programs were consolidated into the 1981 block grants. Together, these approaches helped states replace much of the funding reductions over time. For example, some states carried over funding from the prior categorical programs. States also offset federal funding reductions through transfers among block grants. The transfer option was used infrequently between other block grants, although it was allowed in five of the block grants. States also used their own funds to help offset reduced federal funding but only for certain block grants. In the vast majority of cases, the 13 states increased their contribution to health-related or the Social Services Block Grant programs--areas of long-standing state involvement.

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[4]Block Grants: Federal Data Collection Provisions (GAO/HRD-87-59FS, Feb. 24, 1987).

Initially, most federal funding to states was distributed on the basis of their share of funds received under the prior categorical programs in fiscal year 1981. Such distributions, however, may not be sensitive to populations in need, the relative cost of services in each state, or states' ability to fund program costs. Except for the Social Services and Community Development block grants, a requirement was included in all block grants that the allocation of funds account for the amount states received in previous years to ease the transition to block grants.

Today, most block grants use formulas that more heavily weigh beneficiary population and other need-related factors. For example, the CDBG uses a formula that reflects poverty, overcrowding, age of housing, and other measures of urban deterioration. The formula for Title IIA of the Job Training Partnership Act considers unemployment levels and the number of economically disadvantaged people in the state. This formula is also used to distribute funds to local service delivery areas. However, three block grants--Community Services, Maternal and Child Health, and Preventive Health--are still largely tied to 1981 allocations.

Block grants significantly reduced the number of reports required of recipients compared with those required under previous categorical programs. Despite this, the 13 states we visited generally reported that they were maintaining their prior level of effort for data collection. With block grants, states tailored their efforts to better meet their own planning, budgetary, and legislative needs. Because of their new management responsibilities, states sometimes passed on these reporting requirements to local service providers.

Limited reporting requirements and flexibility allowed states in determining the content of program information and its reporting resulted in inconsistent national information available to the Congress on program activities, services delivered, and clients served. Moreover, this made state-by-state comparisons difficult if not impossible. In response to this situation, in 1984, model criteria and standardized forms were developed for some block grants to collect uniform data primarily through voluntary cooperative efforts by the states. However, the lack of data comparability reduced the usefulness of the data in serving the needs of policymakers for allocating federal funds, determining the needs of individual states, and comparing program effectiveness among states.

Just as with data collection and reporting, the Congress became concerned about financial accountability in federal financial assistance provided to state and local entities. With the passage of the 1984 Single Audit Act, the Congress promoted more uniform, entitywide audit coverage than was achieved under the previous grant-by-grant audit approach. We have found that the single audit approach has contributed to improved financial management practices in state and local areas. Systems for tracking federal funds have been improved, administrative controls over federal programs have been strengthened, and oversight of entities receiving federal funds has increased. However, the single audit process is not well designed to assist federal agencies in program oversight, according to our 1994 review.[5]

For example, we found some limitations with the usefulness of single audit reports. For example, reports do not have to be issued until 13 months after the end of the audit period, a length of time that many federal and state program managers found too late to be useful. In addition, managers are not required to report on the adequacy of their internal control structures, which would assist auditors in evaluating the entity's management of its programs. In addition, the results of the audits are not being summarized or compiled so that oversight officials and program managers can easily access and analyze them to gain programwide perspectives and identify leads for follow-on audit work or program oversight. Yet, we believe that the Single Audit Act is an appropriate means of promoting financial accountability for block grants, particularly if our recommended improvements are implemented.

Even though block grants were intended to increase state flexibility, additional constraints that were placed on block grants over time had the effect of "recategorizing" them. These constraints often consisted of set-asides, requiring a minimum portion of funds to be used for a specific purpose, and cost ceilings, specifying a maximum portion of funds to be used for other purposes. Such constraints reduced states' flexibility. Many of these restrictions were imposed due to congressional concern that states were not adequately meeting national needs. For example, in nine block grants, from fiscal years 1983 and 1991, the Congress added new cost ceilings and set-asides or changed existing ones 58 times.[6] Thirteen of these amendments added new cost ceilings or set-asides to 9 of 11 block grants we reviewed.

LESSONS LEARNED

Our research suggests that experience with the 1981 block grants can teach us three lessons of value to the Congress as it considers creating new block grants. First, focusing on accountability is imperative for results, and GPRA may provide the appropriate framework. Second, funding allocations based on distributions under prior categorical programs may be inequitable because they do not reflect need, ability to pay, and variations in the cost of

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[5] Single Audit Act: Refinements Can Improve Usefulness (GAO/AIMD-94-133, June 21, 1994).

[6] Block Grants: Increases in Set-Asides and Cost Ceilings Since 1982 (GAO/HRD-92-58FS, July 21, 1992).

providing services. Finally, although states managed the transition to the 1981 block grants well, today's challenges are likely to be greater. The programs being considered for inclusion in block grants are not only much larger, but, in some cases, such as Aid to Families With Dependent Children, fundamentally differ from programs included in the 1981 block grants.

Need to Focus on Accountability for Results

One of the principle goals of block grants is to shift responsibility for programs from the federal government to the states. This includes priority setting, program management, and, to some extent, accountability. However, the Congress and the federal agencies maintain an interest in the use and effectiveness of federal funds. Paradoxically, accountability is critical to preserving state flexibility. When the Congress lacks adequate program information, the 1981 block grant experience demonstrates that added funding constraints limit state flexibility and, in effect, recategorize the programs. Across the government, we have recommended a shift in focus of federal management and accountability away from inputs and rules to one of program results and outcomes.[7] This focus on outcomes rather than inputs is particularly appropriate for block grants, given their emphasis on states' flexibility in determining the specific problems to address and strategies to employ in combatting those problems.

GPRA offers an accountability framework for block grants. Consistent with the philosophy underlying block grants, GPRA shifts the focus of federal management and accountability away from inputs, such as budget and staffing levels and adherence to rigid processes, to one on outcomes. GPRA is in its early implementation stages, but by the turn of the century, annual reporting under this act is expected to fill key information needs. GPRA requires every agency to establish performance indicators, set annual performance goals, and report on actual performance in comparison with these goals each March beginning in the year 2000. Agencies are now developing strategic plans (to be submitted by September 30, 1997) articulating their mission, goals, and objectives before meeting these reporting requirements.

Funding Formulas Should Reflect Need and Ability to Pay

The Congress will need to make tough decisions on block grant funding formulas. Public attention is frequently focused on allocation formulas because there will always be winners and losers. Three characteristics of formulas to better target funds include (1)

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[7] Improving Government: Measuring Performance and Acting on Proposals for Change (GAO/T-GGD-93-14, Mar. 23, 1993).

factors that consider state or local need, (2) factors that consider differences among states in the cost of providing services, and (3) factors that consider state or local ability to contribute to program costs. To the extent possible, equitable formulas rely on current and accurate data that measure need and ability to contribute. We have reported on the need for better population data to better target funding to those with the greatest need.[8]

Today's Transition Challenges Likely Greater Than in 1981

The experience managing the 1981 block grants contributed to increased state management expertise. Overall, states learned to respond to public service demands and initiate innovations during the 1980s and 1990s. In addition, beginning in the 1960s and 1970s, states modernized their government structures, hired more highly trained staff, improved financial management practices, and diversified their revenue systems.[9]

State and local governments have also taken on an increasing share of the responsibility for financing this country's domestic expenditures. As figure 2 illustrates, state and local government expenditures have increased more rapidly than federal grants in aid. Between 1978 and 1993, state and local outlays almost doubled, from $493 billion to $884 billion, in constant 1987 dollars.

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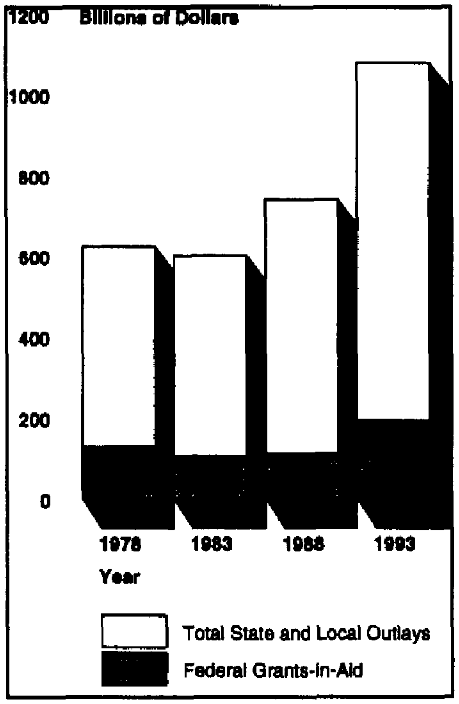
[8] Federal Aid: Revising Poverty Statistics Affects Fairness of Allocation Formulas (GAO/HEHS-94-165, May 20, 1994) and Federal Formula Programs: Outdated Population Data Used to Allocate Most Funds (GAO/HRD-90-145, Sept. 27, 1990).

[9] Federal-State-Local Relations: Trends of the Past Decade and Emerging Issues (GAO/HRD-90-34, Mar. 22, 1990). Other GAO work on intergovernmental trends appears in State and Local Finances: Some Jurisdictions Confronted by Short- and Long-Term Programs (GAO/HRD-94-1, Oct. 6, 1993) and Intergovernmental Relations: Changing Patterns in State and Local Finances (GAO/HRD-92-87FS, Mar. 31, 1992).

Figure 2: State Program Funding Is Increasing



Note: Federal grants in aid and state and local outlays are expressed in inflation-adjusted dollars (1987=100).

Source: U.S. Advisory Committee on Intergovernmental Relations.

Many factors contribute to state fiscal conditions. For example, state officials have expressed concern about unfunded mandates imposed by the federal government. In addition, practices such as "off-budget" transactions could obscure the long-term impact of program costs in some states. While states' financial position has improved on the whole,[10] the fiscal gap between wealthier and poorer states and localities remains significant, in part due to federal budget cuts. We reported in 1993 that Southeastern and Southwestern states, because of greater poverty rates and smaller taxable resources, generally were among the weakest states in fiscal capacity.

New block grant proposals include programs that are much more expansive than block grants created in 1981 and could present a greater challenge for the states to both implement and finance. Nearly 100 programs in five areas--cash welfare, child welfare and

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[10] In 1994, the National Governors' Association and the National Association of State Budget Officers reported that the steadily growing economy has improved state budgets.

abuse programs, child care, social services and food and nutrition-could be combined, accounting for more than $75 billion of a total of about $200 billion in federal grants to state and local governments. The categorical programs, which were replaced by the OBRA block grants, accounted for only about $6.5 billion of the $95 billion 1981 grant appropriations.

In addition, the present block grant proposals include programs that fundamentally differ from those included in the 1981 block grants. For example, AFDC provides direct cash assistance to individuals. Given that states tend to cut services and raise taxes during economic downturns, these cash assistance programs could experience funding reductions that could affect vulnerable populations. Unlike the federal government, state governments have less flexibility to initiate financial measures to counter economic trends. In addition, some experts suggest that states have not always maintained state funding for cash assistance programs in times of fiscal strain.

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Mr. Chairman, that concludes my prepared statement. At this time I will be happy to answer any questions you or other members of the Subcommittee may have.

For information on this testimony, please call Sigurd R. Nilsen, Assistant Director, at (202) 512-7003, or Jacquelyn B. Werth, Evaluator, at (202) 512-7070.

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