

Weld Carter

URBAN DEVELOPMENT AND FEDERAL GRANTS

**Arthur P. Becker
Professor of Economics
University of Wisconsin--Milwaukee**

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INTRODUCTION

The creation of the Department of Housing and Urban Development in 1968 attests to the importance that the Federal Government regards matters concerning urban development. The act establishing the eleventh cabinet rank department transfers to and places in under the jurisdiction of the secretary of the department all of the functions, powers and duties of the Housing and Home Finance Agency, the Federal Housing Administration, the Urban Renewal Administration, Community Facilities Administration, the Public Housing Administration, and the Federal National Mortgage Association.

Section 2 of the act sets forth the purpose of the Federal Government in creating this new department:

"The Congress hereby declares that the general welfare and security of the Nation and the health and living standards of our people require, as a matter of national purpose, sound development of the Nation's communities and metropolitan areas in which the vast majority of its people live and work.

To carry out such purpose, and in recognition of the increasing importance of housing and urban development in our national life, the Congress finds that establishment of an executive department is desirable to achieve the best administration of the principal programs of the Federal Government which provide assistance for housing and for the development of the Nation's communities; to assist the President in achieving maximum coordination of the various Federal activities which have a major effect upon urban, community, suburban, or metropolitan development; to encourage the solution of problems of housing, urban development, and mass transportation through State, county, town, village, or other local and private action, including promotion of interstate, regional, and metropolitan cooperation; to encourage the maximum contributions that may be made by vigorous private homebuilding and mortgage lending industries to housing, urban development, and the national economy; and to provide for full and appropriate consideration, at the national level, of the needs and interests of the Nation's communities and of the people who live and work in them."

The above statement is worthy of quotation because it shows official awareness of urban problems and provides a broad framework within which policy recommendations and programs can be devised. It clearly establishes urban development as a Federal concern towards which the resources of the Federal Government, including grants-in-aid, might be applied in greater measure than at present.

The growth of Federal grants during the 20th Century has been enormous. Federal aids¹ to state and local governments have risen from \$7 millions to \$7.857 billions from 1902 to 1962 (See Table 1). Whereas Federal aids amounted to a mere 1 percent of state and local general revenue in 1902, it amounted to 14 percent in 1962. By 1964 Federal aids had risen to \$9.8 billions and were expected to reach \$10.7 billions for 1965 and \$13.0 billions for the fiscal year ending June 1966.² With the new programs for education, health, conservation, urban development, depressed areas and combatting poverty it seems probable that the trend will not only continue but be accelerated.

Before proceeding further in discussing urban development and Federal grants it is important that we know just what we are considering. The topic may be viewed broadly or narrowly. Broadly viewed it would embrace any grants which had a significant impact on the urban communities of the nation. The effect may be indirect as well as direct and include such systems as categorical welfare payments which raise and maintain urban purchasing power. Broadly viewed, most Federal grants can be construed

¹The vast bulk of which consists of grants.

²The Budget in Brief, Fiscal Year 1966, Bureau of the Budget.

(Washington, 1965), p. 56.

TABLE 12 - TRENDS IN FEDERAL AID RELATIVE TO GENERAL REVENUE OF STATE AND LOCAL GOVERNMENTS AND TO FEDERAL GENERAL EXPENDITURE, 1902-1962

(Dollar amounts, except per capita, in millions)

Fiscal year	State and local General revenue		Federal expenditure		Federal aid as a percent of	
	Amount		Per Capita		Federal aid as a percent of	
	Total	Federal aid %	Total	Federal aid %	State & local General revenue	Federal aid as a percent of Federal general expenditure
1962	\$58,214	\$7,857	\$313.28	\$42.28	14	26
1960	50,505	6,974	280.61	38.75	14	30
1958	41,219	4,865	237.80	28.07	12	26
1956	34,667	3,335	207.26	19.94	10	20
1954	29,012	2,966	178.63	18.26	10	20
1952	25,181	2,566	160.36	16.34	10	21
1950	20,911	2,486	137.86	16.39	12	18
1948	17,250	1,861	117.34	12.39	11	19
1946	12,356	855	87.39	6.05	7	10
1944	10,908	954	78.87	6.89	9	8
1942	10,418	858	77.25	6.36	8	12
1940	9,609	945	72.73	7.15	10	14
1938	9,228	800	71.08	6.16	9	14
1936	8,395	948	65.56	7.40	11	17
1934	7,678	1,016	60.76	8.04	13	25
1932	7,267	232	58.21	1.86	3	12
1922	4,781	108	43.44	0.98	2	8
1913	1,912	12	19.66	0.12	1	2
1902	986	7	12.46	0.09	1	3

n.a. - Not available.

- a. Includes amounts received from the Federal Government for contractual services and shared revenues, as well as Federal grants-in-aid.
- b. Excluding national defense, international affairs and finance, space technology, veterans' benefits and services (except education), and interest on debt.

Source: United States Bureau of the Census, Historical Summary of Governmental Finances in the United States, 1957 Census of Governments, Vol. IV, No. 3; and Governmental Finances in 1962, Oct., 1963.

2. The Role of Equalization in Federal Grants, Advisory Commission on Intergovernmental Relations, (Washington, 1964) P. 14.

as existing?

to assist in urban development. (See Table II)

24p?

The current definition would regard urban development only in terms of activities directly concerned with urban planning and its implementation among these would be such items as low rent public housing, urban renewal, sewerage treatment plants, community facilities, and assistance in mass transportation problems. This would include most of the Federal grants made directly to local governments. (See Table III) It should be noted that even this restricted concept of urban development grants include those that provide service benefits such as educational and health services as well as capital improvements. Moreover, we would have to add grants to states for the purpose of providing highways in urban areas, recreational park areas for urban populations, besides the many activities in which only part of the federal grants are paid to local governments. The Federal government was administering over 40 separate programs of financial aid at the end of 1962. More than half of these were authorized after 1950.⁶

10/10A
10/10B
10/10C

The distinction holds significance in relating existing and proposed programs to urban development objectives. If urban development is viewed broadly, greater latitude is afforded in devising programs to meet its objectives. The position taken here is that it is generally preferable to take the broad view, especially in matters affecting the local economic base and fiscal matters. Transfer payments boost local secondary business activities and yield higher local property tax revenues. The lifting of local welfare burdens by means of Federal grants directly, or indirectly through state governments, has an effect equivalent to an increase in property tax yield. In either case urban local governments are in a better financial position to provide additional capital improvements and services needed for urban development.

Our considerations up to this point are intended to serve as a preamble or framework for the primary purpose of this paper. We are mainly

⁶ Advisory Commission on Intergovernmental Relations, Impact of Federal Urban Development Programs on Local Government Organization and Planning (Washington, 1964)

Table II⁴

FEDERAL GRANTS-IN-AID, BY FUNCTION

No. of Programs	Function	1962 Expenditure (millions)	Percentage Distribution
1	Highways	\$2,743	39.1
7	Public welfare	2,448	34.9
14 *	Education	622	8.9
1	Employment security administration	439	6.2
3 *	Housing and urban renewal	309	4.4
9	Natural resources	165	2.4
14 ***	Health and hospitals	152	2.2
1	Air transportation	57	0.8
10 ***	All other	79	1.1
60	Total	\$7,014	100.0

* Indicates inclusion of one program and *** indicates inclusion of three programs for which no funds were disbursed in fiscal year 1962.

⁴The Role of Equalization in Federal Grants, Advisory Commission on Intergovernmental Relations, (Washington, 1964) p. 28.

TABLE III⁵
FEDERAL GRANTS-IN-AID DIRECTLY TO LOCAL GOVERNMENTS, 1962
(In thousands)

Program	Amount
* Air Pollution	\$ - -
* Airport Construction	32,674 ^{a/}
Area Redevelopment	118
Centers for Research on Mental Retardation ^{b/}	- -
Clinics for Domestic Agricultural Migratory Workers	- -
Community Health Services Project Aid ^{c/}	- -
* Grants for Juvenile Delinquency Prevention and Control	- -
* Health Research Facilities Construction	1,034
* Indian Education and Welfare	1,236 ^{a/}
Low Rent Public Housing	148,674
Mass Transportation Demonstration	75
Maintenance and Operation of Schools in Federally Affected Areas	214,534
* Open Space Land	- -
Research on Maternal and Child Health Services ^{b/}	- -
Research in Education of Handicapped Children ^{b/}	- -
School Construction Assistance in Federally Affected Areas	41,268
University Affiliated Facilities for the Mentally Retarded ^{b/}	- -
Urban Planning Assistance	6,400
Urban Renewal	160,056
* Vaccination Assistance	- -
* Venereal Disease Control (Project) Grants	2,530
Vocational Education: Title III (Training Under ARA)	- -
Vocational Rehabilitation Demonstration Grants ^{c/}	- -
Waste Treatment Construction	41,607

* Only part of these funds are paid directly to local governments.

^{a/} Estimated funds paid direct to local governments in 1962.

^{b/} Programs enacted in 1963 (as of December 10, 1963).

^{c/} Sums not shown separately from over-all grant amount in Treasury Report.

⁵ The Role of Equalization in Federal Grants, Advisory Commission on Intergovernmental Relations, (Washington, 1964) p.26.

concerned with (a) examining the major problems of urban development, broadly defined, (b) examining the causes of urban development problems, (c) noting the conditions of present Federal grants, and (d) recommending changes in conditions and the establishing of some additional conditional grants. Secondly, we will make a few observations in comparing unconditional urban grants with conditional grants and tax credits.

MAJOR PROBLEMS OF URBAN DEVELOPMENT THAT FACE GOVERNMENT

^ Broadly stated, the goal of urban development is to create an urban environment which is compatible with and conducive to bringing out the best in its inhabitants. Human beings seem destined to live close to one another and therefore it is important that urban areas be ^{so} shaped and developed that they will permit man to develop to his highest capabilities in healthy and pleasant surroundings. The kind of urban environment which perfectly fits this prescription has not yet been designed or even conceived. Yet urban man cannot wait for the ultimate blueprint for urban living because it may be forever elusive. The city is a dynamic structure and reflects man's ever changing values, knowledge, machines and practices. In all likelihood man will continue to change and so will his city and his dream of the "ideal city". Meanwhile, each generation is faced with its own problems and attempts to solve them and thereby ^{to} meet the needs of its time. ^ As a result our cities are in a continual process of development.

Urban development has been traditionally and largely private in the United States. The public sector, whether state or local governments, played a role by providing minimum facilities and guidance. However, with the growth of urban areas and their population, the traditional role

of the public sector has been found wanting. Many problems have arisen (for the public sector) most of which can be placed within the following categories:

1. The progressive decay of private and public facilities and the failure to replace them at a speed anywhere near the rate of decay.
2. The inadequate allocation of resources to the public sector.
3. The inadequate standard of public services.
4. "Excessive" disparities in public expenditures, tax burdens, and income.

The decay of private and public facilities outpaces their replacement. Blight and slums grow as cities age and serve the bulk of our population. Most capital, both public and private, avoids rebuilding the central city but flees to the suburbs instead for major new development. Related to the decay of central cities is the concentration within their boundaries of low income and deprived people, deplorable living conditions, despair, lack of motivation, and crime.

The inadequate allocation of resources to the public sector is reflected by our inadequate schools (for special handling of dropouts and provision for vocational training). Traffic congestion attests to the need for better traffic and parking facilities. Air and water pollution require the enactment and enforcement of anti-pollution measures and better incineration, sewerage and water treatment facilities. Parks and open spaces are needed to provide a relaxing and pleasant antidote to the fast pace and closeness of buildings and people. Sometimes essential and desirable services are not provided at all. More often essential public services exist but at levels far below standard.

An important problem confronting urban development problems is the

unsatisfactory standard that prevails for many public services. If that is simply a reflection of the wishes of persons in a local government, there can be no objection unless it harms adjacent urban communities. In many instances this is the case. Slums and blight, for instance, spread their effects beyond the municipality in which they flourish. Zoning for land use and planning cannot be conducted by each municipality independent of adjacent municipalities. Lack of agreement on land use policies, traffic patterns and rivalry for industry and retail trade lead to incompatible land use, a distorted and uneconomic distribution of activities (public and private), lower land values, and a less pleasant and beautiful community.

We also find "excessive" disparities in public expenditures, tax burdens and income among the political units in an urban area and between urban areas. Some of these disparities may not only be justified but desirable if they reflect different scales of public services desired by various local governments. However, some of the disparities are unjustified or fortuitous and continue because there is no present way to remedy the problem. Therefore, a major question of equity arises.

The above list is incomplete and merely suggests some of the economic and fiscal problems with respect to urban development. The private sector can play a role of implementation, but government must play the key role of furnishing guidance and stimulation for the private sector and providing efficiency, equity and essential public facilities. Urban development then, may be viewed as the job of finding solutions to the more critical problems facing urban areas today. Before discussing solutions, however, let us review the causes that have brought about these problems.

THE UNDERLYING CAUSES OF URBAN DEVELOPMENT PROBLEMS

Any attempt to trace urban development problems back to their origin would very quickly lead to the profound population changes that have occurred in urban areas since World War II. First of all there is the great increase in population of urban areas caused by an accelerated migration from rural areas, the post-war resumption of immigration and natural growth due to excess of the birth rates over the death rate. The many millions of additional persons simply could not be contained within the old boundaries of cities. An increasing proportion of total urban population has settled in suburban communities.

The sudden burst of urban population has created an expanded need and demand for customary and new urban development programs. Private and public development both quantitative and qualitative have reached new heights. The burden has been particularly heavy on the public sector because of the abnormal age structure of the population. The percentage of young and old in our urban population has risen to unusually high levels and it is for these age groups that the public sector has special responsibilities in providing schools, hospitals, recreational and other public facilities and services. Simultaneously, the increased public expenditures have had to be shouldered by a smaller percentage of workers, producing a sort of fiscal scissors effect.

Still another population change of great significance to urban development has been the tendency of urban population to segregate itself along economic, social and racial patterns. Central cities are the gathering places of families with low incomes, migrants, immigrants and non-whites. Among these groups are found the highest incidence of deprivation, inadequate education, broken home life and crime. It is hardly surprising that central cities need far more public facilities and services, and much of

that need is desperate. Suburbs, in contrast, attract families that are white, native born, affluent and highly educated. The public facilities and service requirements of suburbs are often at a relatively low level, although some responsibilities are met with relative lavishness as in public education.

While the increasing urban population of the nation settles on the fringes of densely settled urbanized areas, the political boundaries of central cities fail to keep pace. The newly established fringe population is naturally and automatically annexed to the central city both physically and economically. However, it refuses political annexation. Instead, inhabitants of the urban fringe choose to establish their own suburban government and metropolitan governmental fragmentation rises as the tide.

The lack of a general local government over and co-terminous with urbanized areas is a critical deficiency of our present society. An efficient, economical, and free society is one which will respond to the wishes of the people in deciding how economic resources are to be allocated among an endless variety of needs and wants. In the private sector of the economy the decision making structure consists of competitive markets. In the public sector the structure must be democratically constituted and functioning governments. It is only through the latter that a consensus can be arrived at on the amount of resources that should be allocated to the public sector compared with the private sector and how these social goods are to be paid for.

Yet a governmentally fragmented urbanized area cannot arrive at a consensus because of the lack of a political structure whereby this might be achieved. The non-existence of a metropolitan government and its political processes very effectively denies the citizen a voice in

local matters of general concern throughout the urbanized area. The metropolitan citizen faces serious handicaps:

1. He is denied a vote on important matters of general metropolitan concern.
2. He is denied the opportunity of providing or receiving the benefit of the best leadership or counsel throughout the entire urbanized area. (The leaders of a local government do not serve, as a rule, outside of the municipality of their residence.)
3. Many problems are either stifled or inadequately ventilated and debated, resulting in uninformed and emotionally charged citizens throughout the urbanized area.
4. The citizen has no governmental machinery which can provide necessary or desirable public services and the equitable financing of them.

The latter point is of greatest interest to economists and those concerned with government finance. It arises out of the common practice of persons in a metropolitan area to reside in one municipality but work, shop, and receive cultural and recreational services in other municipalities. These various activities require different kinds of public services yet the cost of these services cannot be related to the beneficiaries. Taxes cannot be correlated with benefits, and public service responsibilities cannot be correlated with fiscal capacity. It becomes impossible to establish a consensus on a priority list of public services and allocate taxes justified by the benefits received. In order to overcome this problem each family would have to ~~must~~ carry on all of its major activities in the same community in which it

resides and pays its property taxes. This presents two alternatives:

1. Either urban families would have to move their residence to the municipality in which they are employed and restrict their other major local activities to the same community, or
2. A local political unit providing and financing a number of basic common services must be enlarged or established so that major local activities of its inhabitants will not take them beyond its boundaries.

It has been suggested by Professor Tiebout that governmental fragmentation of an urbanized area is desirable economically because it permits a diversity in quantity and quality of public services to meet the varying tastes and financial capacities of the separate municipalities.⁷ Moreover, it provides a series of options of public service and taxes to a potential resident and thus gives him a freedom of choice. There is a certain degree of merit in the argument and it may justify a limited degree of local autonomy within a metropolitan area. However, this line of reasoning is based upon many unrealistic assumptions. Included are the assumptions that little or no externalities (or spillovers) prevail, the users of urban land possess perfect mobility, that competition among metropolitan communities is rational, and that employment activities do not exist.

Tiebout's analytical model assumes that the inhabitants do not work in the metropolitan area but live off of dividends. A close equivalent for our analysis, although not for our enjoyment, would be the requirement that each person confines his employment and other activities to his resident community. Clearly, this analysis bears no connection with the fundamental

⁷ See Charles Tiebout, "The Pure Theory of Local Government Expenditures", Journal of Political Economy, 64:5 (October, 1956)

economic and social realities of metropolitan living. At best, it may roughly relate to communities that are physically and economically separated.

Another assumption by Tiebout is that competition among communities is rational. If we apply this to industrial firms they would be free to select that metropolitan community which best met its requirements in terms of public services and taxes, assuming other locational considerations to be equal. It is assumed that each municipality will exact charges or taxes to reflect the public services that will benefit the firm and the social costs that the latter will inflict upon the municipality (such as air and water pollution). The fact of the matter is, however, that the competition for industrial firms is so intense between municipalities that they tend to provide abundant industrial services below cost and require little if any compensation from industry for social costs. Industrial firms are in a position to play one municipality against the other and locate in the one whose taxes for which the firm would be liable deviate most from the benefits received and social costs imposed by the firm. This irrational competition between communities in a metropolitan area is possible only because of government fragmentation, and again points to the need for metropolitan government to rationalize benefits and costs. Both of the above assumptions are conditions which cause urban development problems and are simply assumed away by Tiebout.³ Another cause is the external economies and diseconomies between communities in an urbanized area.

A serious external diseconomy already mentioned in the epilogue of

³ See Harvey A. Brazier's "Some Fiscal Implications of Metropolitanism" in City and Suburb, edited by Benjamin Chinitz (1964)

low income, unemployed and troubled families into our central cities. The need for welfare, police, fire, health, and educational services increase and expenditures to support them rise disproportionately for the central city and/or its county (See Table IV) The communities from which the migrants came benefit by the tax savings made possible from a reduction in public services previously rendered. Urban government services providing a great spillover of benefits to residents of adjacent urban communities include public health, hospital, mass transit, arterial urban roads and highways, water supply, sewer and waste disposal facilities, water and air pollution control and facilities, housing and urban renewal.¹⁰

The Advisory Commission on Intergovernmental Relations reports that the social services with the greatest benefit spillovers would probably include:

- Parks and conservation,
- Sanitary and health inspection services,
- Highways and streets
- Planning and zoning,
- Police protection,
- Fire fighting and preventing,
- Judicial functions, including probation and custodial services,
- Civil defense,
- Nuisance control,
- Welfare.

A second group of local services provide substantial spillovers but also permit some direct benefits that are, in most instances, measurable and practically chargeable to the individuals using them:

¹⁰ See Werner Z. Hirsh, "Local Versus Areawide Government Services," (Volume XVII, No. 4) National Tax Journal, December 1964

TABLE 1V9

RELATIONS BETWEEN METROPOLITAN AND SUBURBAN GOVERNMENTS
Central City and Outside City

Standard Metropolitan Statistical Area (In descending population size)	Central City			Outside City		
	Expenditures	Income	Percent expendi- tures to income	Expenditures	Income	Percent expendi- tures to income
		Per Capita			Per Capita	
New York	\$257	\$2,306	11.1	\$259	\$2,734	9.5
Los Angeles	290	2,541	11.4	202	2,422	8.3
Chicago	203	2,294	8.7	141	2,661	5.3
Philadelphia	165	1,875	8.8	138	2,273	6.1
Detroit	202	2,006	10.0	200	2,261	8.8
San Francisco	224	2,534	8.9	230	2,468	9.3
Boston	273	1,916	14.2	182	2,304	8.0
Pittsburgh	188	1,944	9.7	132	1,945	6.8
St. Louis	147	1,801	8.2	125	2,214	5.6
Washington	234	2,403	9.7	148	2,548	5.8
Cleveland	180	1,856	9.7	186	2,784	6.7
Baltimore	199	2,049	9.7	142	1,869	7.6
Newark	243	1,793	13.6	182	2,748	6.6
Minneapolis	186	2,210	8.4	194	2,174	8.9
Buffalo	193	1,910	10.1	210	2,114	9.9
Houston	155	2,063	7.5	187	1,934	9.7
Milwaukee	229	2,105	10.9	210	2,550	8.2
Pat., Clif., Pass.	156	2,104	7.4	156	2,646	5.9
Seattle	174	2,522	6.8	142	2,132	6.7
Dallas	175	2,216	7.9	118	1,965	6.0
Cincinnati	246	2,040	12.1	118	2,153	5.5
Kansas City	157	2,175	7.2	134	2,158	6.2
San Diego	191	2,302	8.3	189	2,050	9.2
Atlanta	158	1,934	8.2	100	1,853	5.4

Source: 1957 Census of Governments; 1960 Census of Population.

9. Advisory Commission on Intergovernmental Relations, Metropolitan Social and Economic Disparities:
Implications for Intergovernmental Relations in Central Cities and Suburbs (Washington: 1964) P.53.

Water supply,

Sewage disposal,

Public health services,

Hospital and medical care facilities

Transportation

Recreation programs,

Education,

Libraries.¹¹

An interesting facet of this problem is that it is often the role of the central city by virtue of its locational advantage to provide metropolitan area-wide public services. A central library, museum, zoo, botanical gardens, police facilities, music hall, and symphony orchestra are examples of this sort of public development. The spillover benefits are widespread, but not the costs. Some of these area-wide activities are not offered by the central city if it is not inclined to shoulder a disproportionate share of the cost. Urban development of such desirable facilities is hampered as a consequence.

Education has major spillover characteristics some of which cancel one another. Central city children who grow up to enjoy affluence move to the suburbs as residents. In general this represents the cream of the educational crop of the central city spilling into the suburbs. On the other hand the central city benefits from highly educated suburbanites working in the city but loses their leadership talents for a multitude of non-business activities, especially governmental. Residents continually move into and out of the metropolitan area creating external economies and

¹¹ Advisory Commission on Intergovernmental Relations, Performance of Urban Functions; Local and Area-wide, (Washington: 1963) Pp. 42-43.

diseconomies. However, the most pronounced character of this simultaneous population movement is the overwhelming educational diseconomies produced by the influx of poorly educated, unemployed or low income families into central cities and the exodus of the affluent and relatively well educated. Washington, D.C. and Chicago illustrate this point very well.

It has been said that neither the problem of governmental fragmentation or economic externalities are significant because the effects of these conditions are taken into consideration by persons and families in deciding where to reside within an urbanized area. It is assumed that low income persons and families would, if they really preferred, move into communities providing higher levels of public services and lower taxes, resulting in lower levels of public services and higher taxes in these communities receiving the low income families. Conversely, the communities losing low income families will be able to provide a higher level of public service to its remaining residents and even enjoy a reduction in taxes. The result of this intra-metropolitan movement would be the equalization of benefits and costs of the communities in the urbanized area. If this goal is not actually reached, the argument continues, it is because of the preferences of residents in being influenced by other matters than public benefits and costs. Thus, residence pattern is a consequence of freely made choices and results in "the best possible of all worlds".

However, once more we meet an assumption that possesses little validity and seemingly less as the days go by. The notion that persons and families are perfectly free to move between municipalities in a metropolitan area is highly unrealistic. It is well known that economic, social, racial and other restraints have operated to create a national pattern of segregation within metropolitan municipalities. Segregation

is becoming more pronounced and central cities are becoming the domain of the deprived, dispossessed and dark. Not all families within a metropolitan area, or even the central city, lack mobility. But it appears that an increasing percentage of families do find themselves trapped in many central cities and it is this disparity in the capacity for mobility that prevents an equalization in benefits and costs by means of migration. Many families would much prefer to move out if they were only financially able. Others, while financially able, cannot find acceptance in any parts of the urban area.

Disparities in the distribution of economic resources stand as yet another major cause of urban development problems. The need for public services bears little relation to the economic resources of a community and it is often those communities having the greatest need for public improvements that find themselves with the lowest fiscal capacity (per capita) with which to meet their needs. The result is the provision of an inferior quality of public facilities and services or none at all.

The disparity of economic resources between communities in a metropolitan area is in part due to the fragmented organization of local jurisdictions. Again we find ourselves confronted with the need of fewer governmental units with broader jurisdiction. This line is equalizing resources and tax burdens. The reorganization of school districts into fewer or wider jurisdictions throughout the nation since World War II has accomplished much in the direction of equalizing economic resources and tax burdens for rural and suburban communities and has produced an amazing construction of educational facilities. The task still remains to equalize burdens between communities in each organized area. The same principle of equalizing burdens applies to those functions, other than education, which are the responsibility of our regular constitutional local governments.

The failure to take advantage of economies of scale in urban development may be due to the relatively small size of some urban communities. A number of services can be expected to offer important economies of scale including air pollution control, sewerage and waste disposal, transportation, power, water, public health services, hospitals, and planning.^{11a} The only possibility that a smaller municipality has to take advantage of these large scale economies is by cooperating with other adjacent municipalities. The barriers to political cooperation on the local level are so great, however that communities are often forced to provide high cost and less efficient service.

Lastly we can refer to fiscal practices and limitations as a major cause of urban development problems. A good example of this point is the already mentioned self-restraint with which local governments deal with their industrial firms and in their attempts to lure new firms. Special air and water pollution control and treatment facilities may be needed. Yet local communities are afraid to require them and have the firms bear the financial burden as they properly should. Inadequate control and treatment facilities are the result.

Taxing and borrowing limitations frequently curb urban communities in developing such needed facilities. These limitations are often obsolete in that they are tied to property assessments which have fallen behind increases in property values. Basically, however, such limitations are most serious where the total value of taxable property in a community is much lower than in adjacent communities.

Another limitation or restriction may be the result of a shared tax program (as in Wisconsin) in which state taxes are shared with communities on the basis of income earned by their residents. Under this arrangement the communities with abundant economic resources (per capita)

^{11a} See Werner S. Hirsch, *Op. cit.*

usually get the largest tax share (per capita) while the lower wealth communities get the smallest share. The revenue limitations of the poorer communities are accordingly reinforced, and needed development programs may have to be forgotten.

The above analysis presented a number of the basic causes of problems and obstacles in the urban development of public facilities and services. They were included the following:

1. Demographic and population changes.
2. Metropolitan government fragmentation.
3. The splitter of benefits and costs beyond the borders of local governments.
4. Disparities in the ability of urban population.
5. Disparities in the distribution of economic resources and fiscal capacity.
6. The failure to take advantage of economies of scale.
7. Fiscal practices and institutions.

We shall now make a few observations regarding the present federal grant program and then make several recommendations.

FEDERAL GRANTS

The subject of Federal grants is many sided and detailed. A great deal has been written on the subject and no attempt will be made here even to summarize all the important and interesting aspects of Federal grants. We will only point out some of the characterizing features which will have a bearing on the recommendations that will be made at the end of this paper.

Conditional grants -- Federal grants-in-aid programs are provided for conditional grants in that they are tied to state or local actions, specific programs, minimum standards of facilities, services, and administration or other requirements. The obvious purpose is to stimulate states and local governments to establish or participate in a variety of programs and to provide support for these programs. It is generally recognized that the stimulatory effects of federal grants is a powerful tool in getting state and local governments to provide needed public services. In 1962 State and local governments provided an estimated \$3 billion to match the \$7 billion Federal grants-in-aid distributed.¹² Once begun these programs often receive state and local financial support (illus. - maternal and child health services, crippled children's services, and child welfare services) beyond that required by the Federal grant program.¹³

¹² Advisory Commission on Intergovernmental Relations, The Role of Equalization in Federal Grants (Washington, 1964) p. 19.

¹³ I. W. Labowitz, Stimulative Effect of Federal Grants-in-Aid: Some Illustrative Data, Library of Congress, Legislative Reference Service, July, 1958.

Block grants which have been proposed by some would loosen, although not remove, the conditions for grant eligibility. As a consequence, grants could be less effective in stimulating the achievement of specific national objectives.¹⁴ Unconditional grants, such as contained in the Hall/Per-
Pechman proposal of sharing the federal income tax, presumably would re-
turn funds to states on the basis of some formula (including perhaps popu-
lation, fiscal capacity, and fiscal effort) with no strings attached as
to how the funds were to be spent.

Conditional grants, block grants, and shared taxes all serve the
allocation function¹⁵ by channeling a larger share of total resources into
the public sector than would occur without any of these devices. However,
there is a difference of degree in the probable success of each approach.
A system of conditional grants, particularly when tied to matching require-
ments, exerts the greatest allocation (to the public sector) effort whereas
shared taxes would likely have the least allocation influence. State and
local governments receiving unconditional grants may choose to cut taxes
rather than increase expenditures, although pressures to spend may not
allow complete revenue substitution.

Most grants are indirect — Federal grants-in-aid are made to state
governments as a rule rather than directly to local governments. In 1962
localities received about \$650 million (See Table III) directly from the

¹⁴ Selma J. Mushkin, "Barriers to a System of Federal Grants-in-aid,"
(Volume XLII, No. 3) National Tax Journal, September 1960.

¹⁵ See Richard A. Musgrave, The Theory of Public Finance, (New York,
1959).

federal government. A variety of interpretations can be placed on this procedural.

1. It is in accord with the tradition of States wishing to retain control over their own legislation. States may feel that their control over local government is weakened if the latter can bypass state governments completely in dealing with the Federal government.
2. It permits the States a degree of flexibility and initiative in implementing the grant programs in a manner best adapted to its own conditions.
3. It reflects the difficulties of establishing a general purpose metropolitan government or simply separate metropolitan districts each of which is responsible for a specific local government function. The jurisdictional limitations of local government may leave no viable alternative but for the state to handle such programs. The administrative limitations of many local governments adds another dimension to this problem. Local governments often are not in a position to accept the administrative responsibility involved in carrying out the grant by setting its conditions.

perhaps all three explanations contribute to the fact that direct aid to local governments is relatively small.

No unified policy to achieve equalization -- With the influence of cheap urban living, improved mass communication and transportation facilities the public service requirements of urban communities are rising and becoming more uniform. However these demands do nothing to generate higher and

more urban revenue resources. In fact the disparities in tax burdens tend to become aggravated and political pressures arise with the purpose of halting the tendency toward greater disparities. In addition the achievement of greater equalization among urban communities is demanded. Assuming similar expenditures for public improvements and services, the disparity in tax burdens among urban communities is due to two underlying factors: the fiscal capacity (revenue resources) of each community and its tax effort (the degree to which it actually taps its revenue resources).

Federal grants-in-aid have been proposed to assist in equalization by varying the size of grants inversely with fiscal capacity and directly with its efforts (by increased taxes) to help itself and with its needs. The Advisory Commission on Intergovernmental Relations has studied various measures of fiscal capacity and effort for intergovernmental tax and grant-in-aid policies.¹⁶ The Federal government has settled on personal income in each state as the measure of its relative fiscal capacity.

The older Federal grant programs rarely included equalization features, however equalization has been assigned a significant role in the newer programs enacted since World War II. It must be mentioned that the purpose of equalization by Federal grants is not equalization per se but the achievement of national objectives, such as minimizing levels of essential public service through cooperative effort of State and local governments.

¹⁶ See Advisory Commission on Intergovernmental Relations, The Role of Equalization in Federal Grants (Washington, 1964).

with the Federal government.¹⁷ However the role in equalization through Federal grants has been highly vicissitudinal, inconsistent and reflects the lack of agreement as to the degree of importance that should be assigned to interstate needs and finite resources. The traditional desire of each State to determine its own needs and programs and to resist greater dependency upon the Federal government may explain why no consensus has been forthcoming.

A unified policy or organization to coordinate urban development -- A recent study by the Advisory Commission on Intergovernmental Relations found no evidence "to indicate the existence of a unified Federal policy or organizational machinery for coordinating aid programs in the field of urban development."¹⁸ This state of affairs reveals a serious short-coming of Federal grant programs designed to assist in urban development. As may note the following illustrations of this problem:

1. Many Federal programs such as highway development, urban renewal, public housing, and the encouragement of economic growth are interdependent. Failure to coordinate these programs may cause one to hinder out the benefits of another. Coordination of programs not only avoids the loss of program benefits but might occasionally allow the materializing of mutually beneficial programs (a case in which the whole is greater than the sum of its parts).

¹⁷ Ibid., p. 10.

¹⁸ Advisory Commission on Intergovernmental Relations, Impact of Federal Urban Development Programs on Local Government Organization and Planning (Washington, 1964) p. 33.

2. Federal urban development programs are less effective because of the multiplicity of local governments in urban areas. Many of these governments are not equal to the task of preparing detailed and realistic plans for their development and for carrying out these plans (para. 2). Yet are these local governments able to coordinate a long-term program to maximize their actual benefits? The local presence and contribution by Federal employees is a possible solution to the problem, but that would be too costly and constitute too direct an intrusion into state and local affairs to be acceptable.
3. Sometimes Federally assisted development programs are less effective and produce fewer benefits if fragmented among local government jurisdictions in any urban area. The planning and location of facilities in each of a variety of programs, such as public water and sewerage facilities, mass transit, highways, hospitals, schools, airports and medical facilities must be related in an orderly way to best serve the entire urban population in terms of efficiency, economy and quality of service.
4. Some Federal urban development programs do not permit, facilitate, or encourage joint efforts of local governments in the same urban area in dealing with area-wide needs. Major area-wide urban functions include transportation, water supply, sewerage disposal, land use planning and comprehensive planning.
5. Many Federal programs encourage the use of special districts, authorities and other institutional arrangements rather than general purpose local governments. The creation of many separate

and the other hand, have given rise to a number of problems, such as
the reduction of the number of people working in the public sector,
the reduction of the number of people working in the private sector,
or the reduction of the number of people working in the public sector,
and the reduction of the number of people working in the private sector.

Some Federal urban development programs are so rigidly specified
as to prevent proper, proper local governments from helping and
organizing themselves administratively and legislatively to best
carry out the programs under special local conditions.

The importance of the Federal government's role in coordination of the
local **level** cannot be over emphasized for the future development of urban
areas. The reason for this lies not throughout this paper and many studies
some of which have been cited. During studies the problems of urban com-
munities, urban development, and some aspects of the role of the Federal
government in urban development, we shall now turn to the more
recent studies pertaining to Federal grants for urban development.

CONCLUSIONS AND RECOMMENDATIONS

The viewpoint taken here is that of maximizing use of Federal grants
toward the goal of achieving rather than other social welfare.
It is difficult for State and local governments to raise the reputation
of Federal grants. For allocation of additional resources to the public
sector will be preferred by a local government when the marginal social
benefits of an urban development project exceed the marginal local costs
to the community. Where the marginal social benefits are greater than
the marginal local costs, the local government will have an
opportunity for social benefits without additional local social costs.
State and local matching requirements furnish some of the mechanism but

a grant still reduces the community's direct social cost down to its matching contribution. The result is an allocation of resources to a development project which a locality refuses to support alone because, by its own evaluation, costs exceed benefits.

Moreover, the establishment of grant programs to achieve national objectives requires Congress to make normative judgements as to what local government services are in the national interest even though the social costs for some communities exceed their benefits. Forcing localities to ^{accept} ~~provide~~ urban development norms at little or no marginal costs to them raises grave questions. One such question pertains to the validity of normative judgements by the Federal government which is so far removed from local governments. Greater confidence should be held for social values if they reflected a consensus of the population throughout each urbanized area.

We can now draw the following conclusions from our analysis:

1. Effective area-wide governments would allow urbanized areas to solve many of their own development problems and make their own decisions on public services and their financing without the interposition of the Federal government. This should allow maximum local control, citizen participation, and accessibility to the residents of each area. The public sector must depend upon these conditions for the economic allocation of resources just as the private sector of the economy depends upon free and competitive market conditions.
2. An urban area-wide government need not completely displace traditional local governments. However, it should have a wide enough jurisdiction and assume appropriate local public services:
 - a. So that the benefits from its services will be enjoyed primarily within its jurisdiction. In this way, major

spillovers or externalities of local public services can be reduced and persons enjoying public services will have to share their costs. Enlarging the local jurisdiction could also compensate for the immobility of many residents within the area.

- b. To permit the realization of economies of scale.
 - c. To make resources available for establishing necessary public services (in terms of financing, legal and administrative abilities) **at** an adequate level or quality of services throughout the urbanized area.
 - d. To permit effective performance (in terms of planning, financing, technical and social requirements) of public services.
 - e. To permit rational competition between localities within the urbanized area.
 - f. To permit maximum use of human resources for solving area-wide problems.
 - g. To reduce disparities in revenue resources and tax burdens of localities within the urbanized area.
3. Any area-wide government should be at least a multi-purpose, if not a general purpose, government. This is required if its citizens are to be given an effective opportunity to establish priorities, resolve conflicting interests, and balance government needs with resources. This opportunity is denied local citizens if increasing numbers of single purpose districts are simply piled on top of each other. The multi-purpose district is a necessary condition for the public sector to function economically.

and the Federal Government should be encouraged to continue to support the development of the urban areas.

4. Federal grants should be used to support the development of the urban areas and to provide for the development of the urban areas.

Development should be abandoned, preventive measures implicit in 1 to 3 above) should receive greater attention by both State and Federal governments.

The above conclusions have led us to the following recommendations on urban development and Federal grants:

1. Federal grants should be provided for and administered so as to stimulate State governments and urban voters to establish and organize suitable area-wide local governments that:
 - a. would each embrace an entire urbanized area,
 - b. have flexible boundaries (to permit expansion) that are co-terminous with their physical and economic urbanized areas,
 - c. would serve as a single multi-service government in each area, and
 - d. can be adapted in terms of organization and administration to meet special local and state conditions.
2. Federal grants should be used to support those urban functions of an area-wide local government if:
 - a. Congress decides that minimum standards and widespread application of these public services are in the national interest,
 - b. major spillover problems of area-wide government services occur and it (the area-wide government) is judged the best administrative unit for rendering those services.

3. Federal grants should be used to encourage the transference of local services to the respective states where spillover, equity, and other pertinent considerations cannot be satisfied even though an area-wide local government assumed these functions.¹⁹

These recommendations are made in full awareness of their controversial nature and past difficulties in accomplishing very much, especially attempts in establishing metropolitan governments. However, the new resolve of Congress in creating the Department of Housing and Urban Development (quoted at the beginning of this paper) raises new hope that the Federal government will lend its influence in helping materialize these past dreams.

¹⁹ The above recommendations are not intended to be comprehensive. Among other things, they do not deal with fiscal capacity and effort, and equalization through specific grants. The tailoring of specific Federal grants to fiscal capacity and effort, and attempts at equalizing local tax burdens may weaken incentives to establish area-wide urban governments. The approach recommended here would spread out local revenue capacity, even out fiscal effort and equalize tax burdens in a fundamental way. The grant approach would seem to perpetuate structural and functional inadequacies of government and perhaps ought to be used only as a last resort if attempts to remove the cause of the problem fail. In the meantime, equalization features of grants might be used sparingly.